

Takeover and merger regulation in the United Kingdom and Germany

- A comparative analysis -

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Assessor iur.

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Michael N. Roos

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by

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Abstract

The aim of this study was to undertake a comparative analysis of the regulatory frameworks of takeovers and mergers in their respective legal, economic and cultural context in Britain and Germany. Particular emphasis was given to the regulation and handling of cross-border transactions and the developments on European level.

The first chapters of this thesis examine the regulation and practice of public takeover bids contrasting the well-proven self-regulatory system established under the British City Code with the regulatory developments in Germany, inter alia, the newly introduced voluntary German Takeover Code 1995. With respect to cross border transactions, legal and cultural barriers obstructing a level playing field for (hostile) takeover offers are considered in detail. In this context various features of German corporate culture which are identified as barriers and have no equivalent in Britain, such as the two-tier board system, the extensive employee representation on supervisory board level and the role of the banks are analysed. On European level, the 1996 proposal for a new Takeover Directive is discussed critically. Those provisions of the proposed 5th Structures Directive designed to tackle barriers to takeovers are considered.

The second major subdivision of this study deals with the policing of takeovers and mergers from a competition law perspective. Highlighting the differences in the understanding of what constitutes merger control in Britain and Germany, the institutional structures as well as the substantive

merger control criteria applied by the national authorities are compared. In the context of the European Merger Regulation particular emphasis is given to the demarcation of jurisdiction between the national merger control authorities and the Merger Task Force of DG IV in Brussels.

It is submitted that this study has contributed to the understanding of why there is no level playing field for public takeover bids. Suggestions have been made as to how some of the barriers could be removed through legislative measures both on German and European level. It is further submitted that this thesis has contributed to the understanding of the differing concepts underlying merger control in Britain and Germany and that it has highlighted the challenges to the national merger control authorities deriving from an ever increasing internationalization of markets.

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PART ONE

Introduction

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Chapter 1

INTRODUCTORY REMARKS

The evolution of takeover and merger regulation as a new field of law dating back to the mid 1960s is one of the most conspicuous developments in the wider field of company and competition law in postwar Britain. With more than 6.000 announced takeover bids having been handled by the British Takeover Panel, Britain is the undisputed European leader in the regulation of public takeover offers. This situation is sharply contrasted by the state of affairs in Germany where “real” Anglo-style public takeover offers play at best a very limited role in practice.¹

In recent years the ever increasing internationalization of business, more specifically the European integration with its concept of a *common market*, has added a new international dimension to takeover and merger regulation. Foreign bidders are frequently behind public takeover offers for British public companies. Against this scenario the question has repeatedly been raised whether British companies do have an equal chance to acquire abroad through public bids. In other words, is there a level playing field for takeover bids? Germany is often quoted as a jurisdiction in relation to which reciprocity does not exist.

1 For an empirical study see *Wymeersch*, Unternehmensführung in Westeuropa, AG 1995, 299, 307. Also *Krause*, Zur Gleichbehandlung der Aktionäre bei Übernahmeangeboten und Beteiligungserwerb WM 1996, 845; *Neye*, Der neue Übernahmekodex, ZIP 1995, 1464; *Thoma*, Der neue Übernahmekodex der Börsensachverständigenkommission, Osnabrück, Arbeitspapier 9/96, p. 4.

Partly due to the process of internationalization and integration, takeover and merger regulation is the subject of considerable debate in Britain, Germany, and on European level as recent regulatory initiatives, which will be discussed in this thesis, demonstrate. In Britain, a far reaching debate on a competition law reform is going on and to some extent reflected in the Reports by the Trade and Industry Committee on Takeovers and Mergers in 1991 and on Monopolies in 1995. In Germany, a new voluntary Takeover Code was introduced in 1995 and a recent government proposal for a competition law reform is designed to bring German law more in line with European law. On European level, the European Merger Regulation, which entered into force in 1990, commenced a new chapter in the history of European competition law. Recently, a *Green Paper* on the Review of the Merger Regulation (1996) was published by the Commission. Moreover, in 1996 the Commission presented a new proposal for a Takeover Directive.

Chapters 3 to 6 of this thesis undertake to analyse and compare the respective regulatory takeover frameworks in Britain and Germany, the respective corporate culture which is reflected in these rules, and the legal and/or cultural barriers which allegedly obstruct the desired level playing field. The focus will be on bids for publicly listed companies as those companies are the most likely targets of public takeover bids. Emphasis will also be given to European developments, most notably the 1996 proposal for a Takeover Directive. The need and desirability of such a Directive will be discussed critically.

Chapters 7 to 9 are devoted to a comparative analysis of merger control law as this field is of equally pre-eminent importance to any potential bidder. Clearly, with the entering into force of the European Merger Regulation in 1990 a new era in merger control resulting in the co-existence of national and directly applicable European rules has begun. *Rumour has it* that the German merger control regime

exercised by the Federal Cartel Office in Berlin is rather strict, scaring off potential bidders, while the British and European authorities are rather liberal and lenient. The thesis will deal with this question.

An APPENDIX contains some German and European material which might otherwise not be readily available to a British reader.

Chapter 2

ECONOMIC BACKGROUND

Before embarking on the legal analysis of the regulatory framework of takeover and merger control in the U.K. and Germany, it seems useful to provide some basic statistical data with regard to Anglo-German cross-border mergers and acquisitions.

Table 1 at page 18 shows the number of Anglo-German mergers and acquisitions from 1990 to 1992. It is interesting to note that cross-border transactions between the U.K. and Germany were biased in favour of the U.K. by 116. Hence, British companies appear to be the more active buyers. However, the vast majority of these Anglo-German acquisitions involve privately negotiated (friendly) deals where the German target is a privat limited company rather than a public stock corporation.¹ The acquisition of private companies, however, is not the subject of this thesis.

In terms of direct foreign investment Germany invests more in Britain than the other way round. In 1995 Britain was the biggest recipient of German foreign direct investment.² In that year more than a fifth of the DM 48 billion of new German investment abroad went to the U.K. With an inflow of DM 10.64 billion Britain was well ahead of France, the second most popular target for German investment. British direct investment in Germany, in contrast, totalled DM 2.74 billion. The substantial difference in the amounts of direct Anglo-German investment is partly due to the larger gross domestic

1 *Trade and Industry Committee, Takeovers*, para 19; *Begg, Corporate Acquisitions*, para 2.06.

2 See *Financial Times and Frankfurter Allgemeine Zeitung*, 25 May 1996.

product of Germany of ECU 1390.80 billion compared to ECU 800.85 billion of Britain.³ The main reasons, however, are economic. Britain is increasingly seen as an effective alternative to high costs and slow growth in Germany. The main attractions of Britain, as repeatedly stated by German business leaders, include a more flexible workforce due to less rigorous labour law, lower labour and social costs, lower rates of taxation, good international communications and infrastructure, high quality financial and legal services, and, of course, a position inside the European Union.⁴ Prominent examples of German blue-chip investment in Britain during the time of writing this work include *BMW*, which bought *Rover* for £900 million in 1994 and has since announced an investment programme worth £500 million a year, and *Siemens*, the electrical engineering group, which started building a £1 billion semiconductor plant in north-east England.

Table 1: M & A Transactions in 1990-1992

Bidder ./ Target	British Target	German Target	E.U. Target
British Bidder	3.190	193	348
German bidder	77	2.897	626
E.U. bidder	408	642	2.727

Source: European Commission, European Economy, No. 57, 1994

3 Figures of 1994 provided by Eurostat, Eurostatistics, 3/4/5-1996, p. 49.
4 See *Financial Times*, 30 April 1996: Bernd Pischetsrieder, BMW's chief executive, said: "The U.K. currently is the most attractive country among all European locations for the production of cars." Jürgen Gehrels, chief executive of Siemens U.K., is quoted as saying: "We could run a factory in Germany as flexibly as in the U.K., but we would need special permission for such things as seven-days-a-week working and 24-hours-a-day working."

One of the most notable differences between the British and German economy of relevance to the subject matter of this work, relates to the corporate financing traditions in the U.K. and Germany. Generally speaking, the financing of German stock corporations relies heavily on long term bank loans and on debentures rather than equity capital⁵ and only about 3600 stock corporations (Aktiengesellschaften), listed and unlisted included, exist.⁶ The average age of German companies coming to the German stock market is 55 years, against 14 in the U.S. and only eight in Britain.⁷ The number of *domestic listed* public companies in Germany, which would be the prime target for takeover bids, is significantly lower than in Britain as Table 2 below indicates (678 against 1.807).

Table 2: Stock Market Comparisons (1995)

	United Kingdom	Germany
Listed Plc's (overall)	2.336	1.622
Listed Plc's (domestic)	1.807	678
Listed Plc's (overseas)	529	944
New Listings 1995 (overall)	221	188
New Listings 1995 (domestic)	184	20
New Listings 1995 (overseas)	37	168
Turnover Equity, DM million (overall)	1.664.493	1.733.200
Turnover Equity, DM million (domestic)	751.258	1.691.644
Turnover Equity, DM million (overseas)	913.235	41.556

Source: Deutsche Börse, Fact Book 1995

5 Hopt, European Takeover Regulation, in European Takeovers, p. 169.
6 AG-Report 1995, R 272.
7 Financial Times, 16 July 1996.

Rather than the stock corporation, the predominant form of business organisation for medium size firms in Germany is the private limited company (Gesellschaft mit beschränkter Haftung = GmbH), of which more than half a million exist.⁸ Trading in GmbH-shares, however, does not normally take place as it is restricted in a number of ways. Even large GmbH's do seldom have more than a few dozen shareholders and the transfer of shares is very often made conditional upon approval by a simple or special majority of the shareholders.⁹ Besides, both the transfer of shares in GmbH's itself and any contract regarding the transfer of those shares must be notarised by a notary which is a costly procedure.¹⁰

The relatively limited role of the stock market is mirrored by the distribution of the German household savings. Only about 5.5 per cent of the German household savings in 1992 were invested in shares whereas 46.9 per cent went into bank-deposits, 18.0 per cent in bonds and 26.3 per cent in insurance and pension plans.¹¹ Among the general public, there has been a widespread suspicion about shares in Germany as they are considered speculative investments.

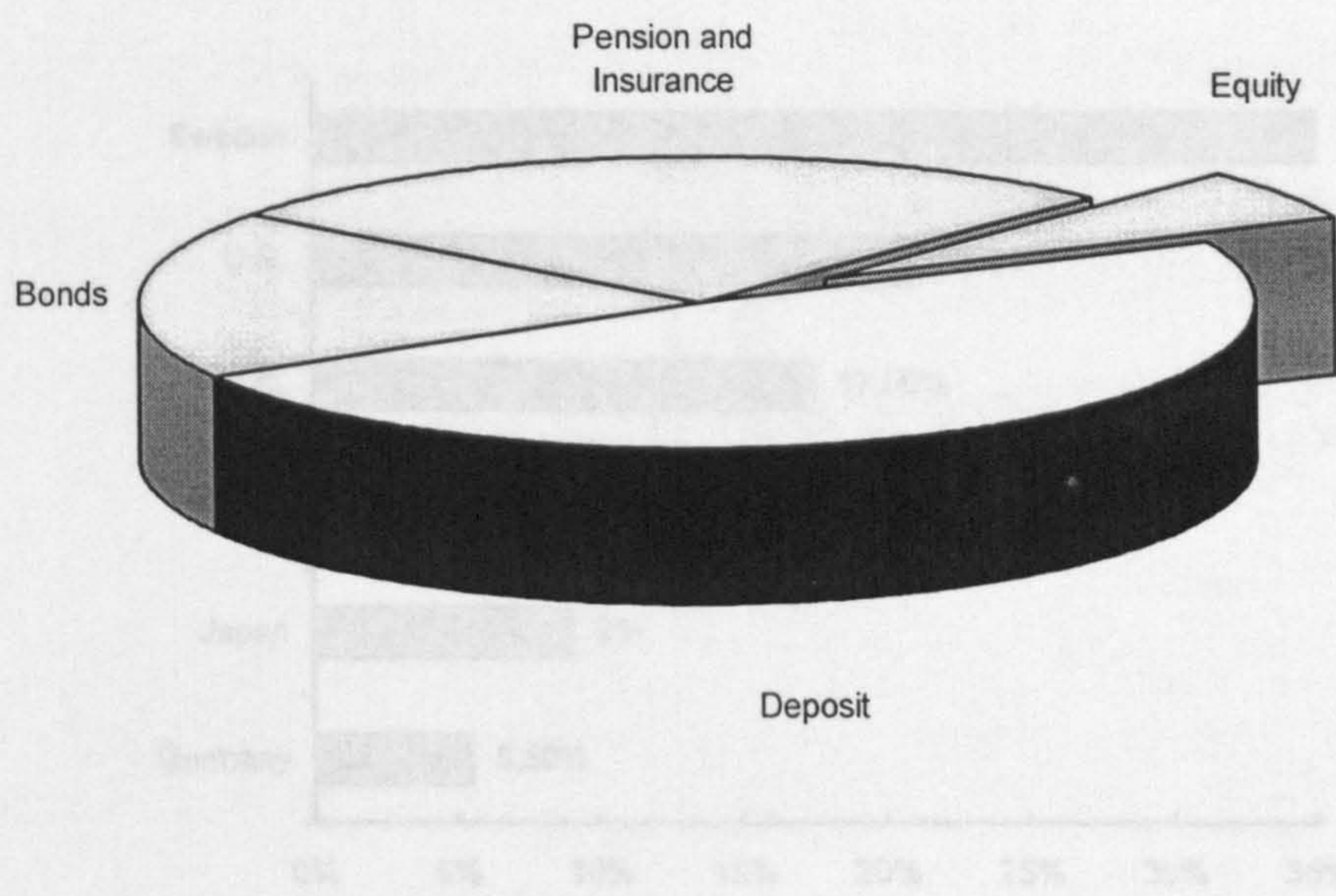
8 *AG-Report* 1993, R 65.

9 The GmbH's are governed by a special Act, the GmbH-Gesetz, which is very different from the Aktiengesetz (Stock Corporations Act 1965) which regulates stock corporations. As a rule of thumb, the GmbH-Gesetz allows for much more flexibility than the Aktiengesetz. The various forms of Partnerships are governed by the Handelsgesetzbuch (Commerce Act 1887) and the foundation of all company law is laid by the Civil Code 1900.

10 Sec. 15 GmbHG.

11 *European Commission*, The Economic and Financial Situation in Germany, p. 150.

Table 3: German Household Savings



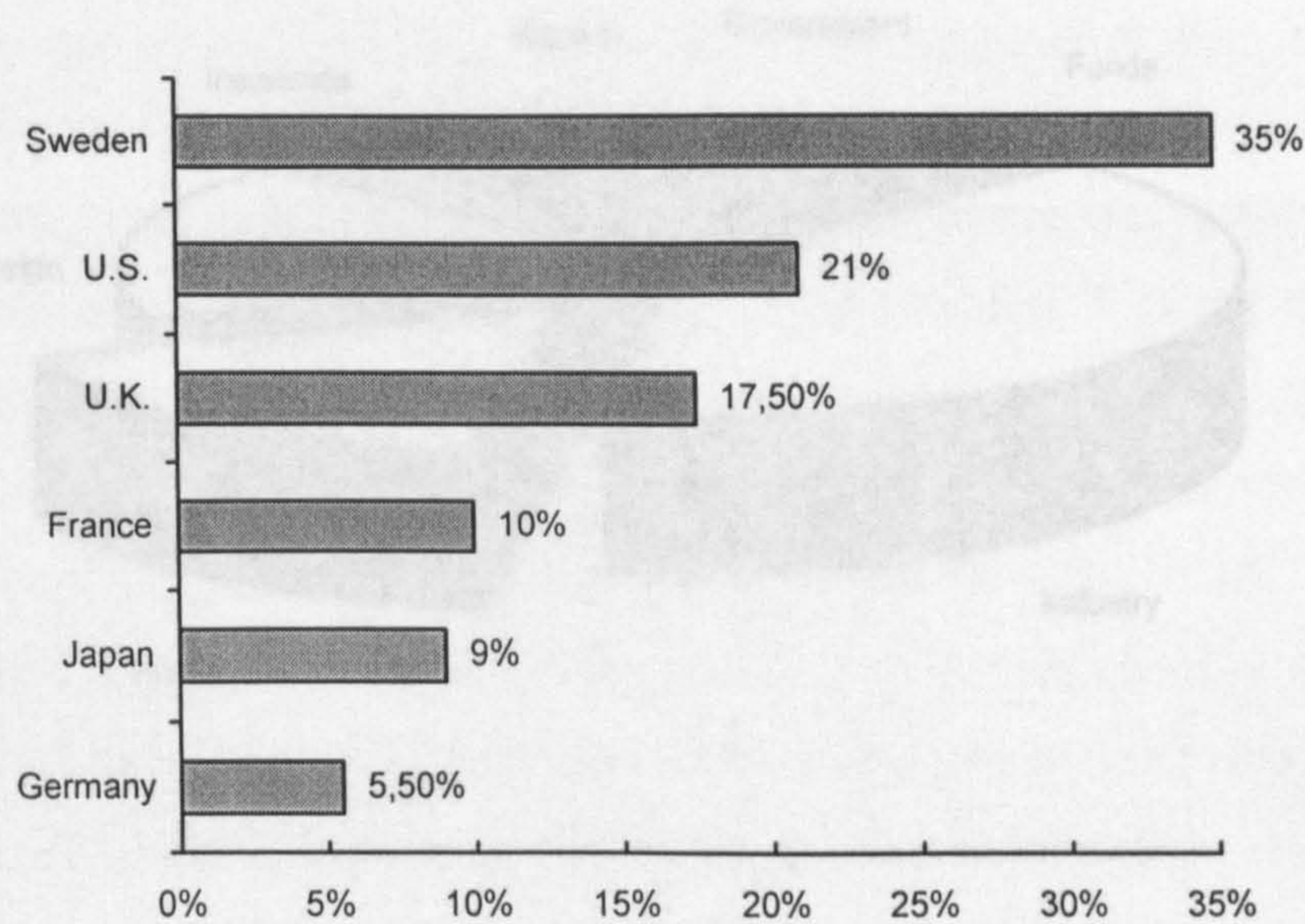
Therefore, the number of shares owned by private investors is rather modest in Germany compared to other leading industrial nations including Britain:¹²

At the end of 1984, about 30.8 per cent of the shares in stock corporations were held by industry, 17.5 per cent by foreign investors, 17.3 per cent by private investors, 8.4 per cent by banks, 6.7 per cent by the government, 5.4 per cent by investment funds, and 5.2 per cent by insurance companies.¹⁴

¹² For an in-depth empirical study of the role of institutional investors in Germany see: Baum-Fraser, 'Institutionelle Anleger und Unternehmenspolitik Eine empirische Untersuchung', AG 1985, 97-112.

¹⁴ See also D.F. Garner to Table 9 in the Data taken from *Financial Times*, 16 July 1996.

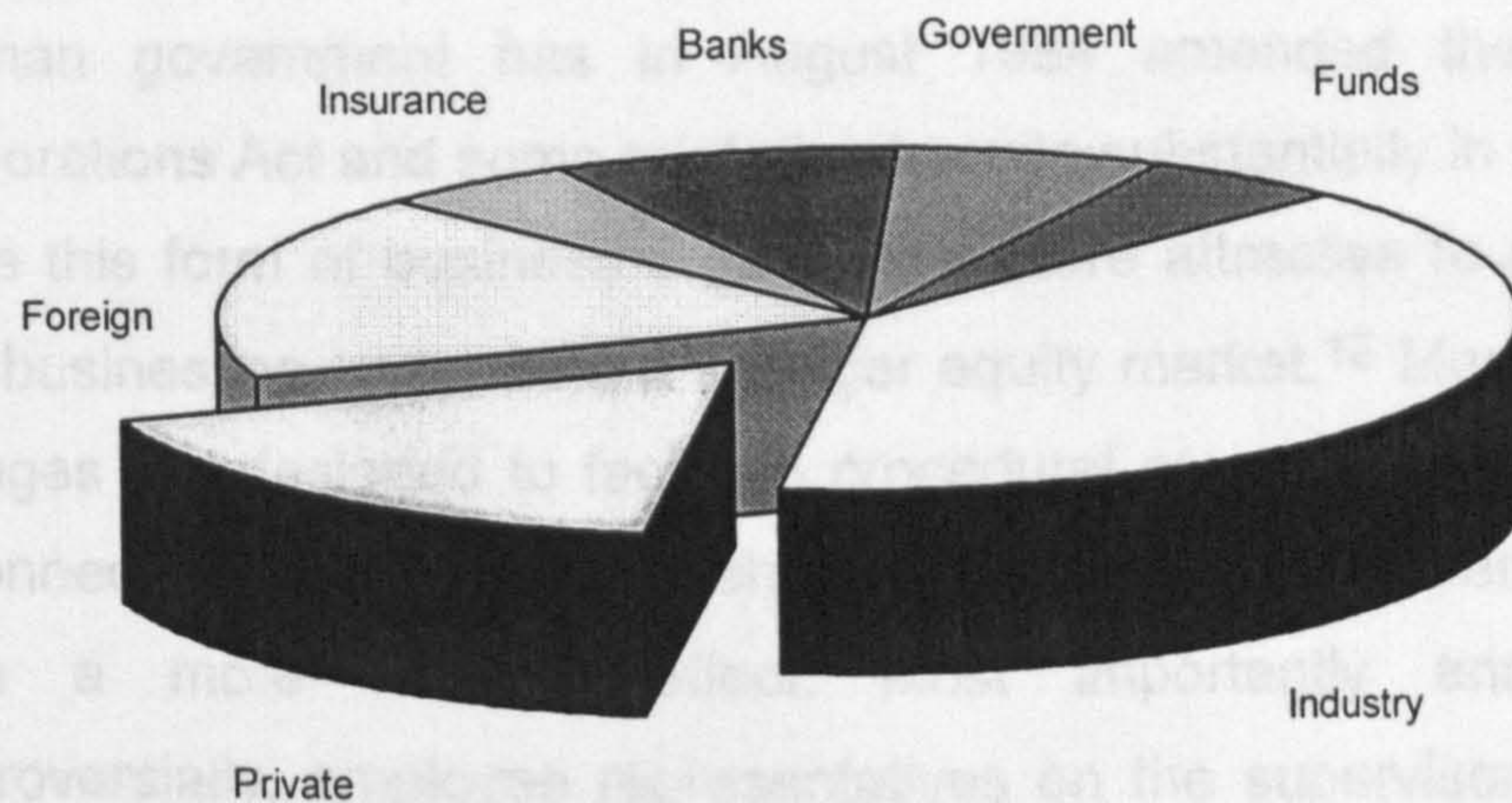
Table 4: Private Share Ownership in leading Industrial Nations



Unlike the U.K., pension funds do not play a major role as a basically government-provided pension system exists in Germany.¹³ At the end of 1994 about 39.6 per cent of the shares in stock corporations were held by industry, 17.5 per cent by foreign investors, 17.3 per cent by private investors, 8.4 per cent by banks, 6.7 per cent by the government, 5.4 per cent by investment funds, and 5.2 per cent by insurance companies.¹⁴

13 For an in-depth empirical study of the role of institutional investors in Germany see *Baums/Fraune, Institutionelle Anleger und Publikumsgesellschaft: Eine empirische Untersuchung*, AG 1995, 97-112.
14 *AG-Report* 1995, R 418. See also *DTI, Barriers to Takeovers in the European Community*, 1990, Volume 2, p. 19.

Table 5: Share Ownership in Germany



However, the number of stock corporations has been increasing steadily in Germany, as Table 6 at page 25 demonstrates, and will continue to do so for various reasons.¹⁵ One reason is the reunification of East and West Germany in 1989. Until 1992 about 200 new stock corporations were floated in the former East Germany, many of them were converted from previously state-owned industries.¹⁶ Another reason is the generational change in the ownership structure of companies. Many companies in Germany were formed during the "*Wirtschaftswunder*" days in the late 1940s and 1950s when Germany was rebuilt after World War II. These companies are traditionally either partnerships or private limited companies controlled by family members. With the postwar founder-generation nearing retirement and the businesses often having

¹⁵ As to the new Securities Trading Act 1994 which is designed to boost investor confidence see 4.1.2.(2) at page 125.

¹⁶ AG-Report 1993, R 64.

reached a considerable size, the question of succession frequently is a problem which increasingly leads to the conversion into stock corporations.¹⁷ Albeit family members may still be the major shareholders in these stock corporations, the foundations for a further diversification in the ownership structure are laid which will in the long run lead to a more open capital market. Furthermore, the German government has in August 1994 amended the Stock Corporations Act and some related acts quite substantially in order to make this form of business organisation more attractive to medium size businesses and create a stronger equity market.¹⁸ Many of the changes are designed to facilitate procedural aspects, for instance, in connection with general shareholder meetings. Other amendments have a more material effect. Most importantly and most controversially, employee representatives on the supervisory board of stock corporations with less than 500 employees are not any more required for newly floated stock corporations.¹⁹ With this change, one of the reasons to choose the form of a private limited company, where no employee representation is required in these circumstances, has gone. Although it is too early to have any evidence on the effect of these amendments, it is widely expected that medium size businesses with less than 500 employees will increasingly turn to the stock corporation as a form of incorporation.²⁰

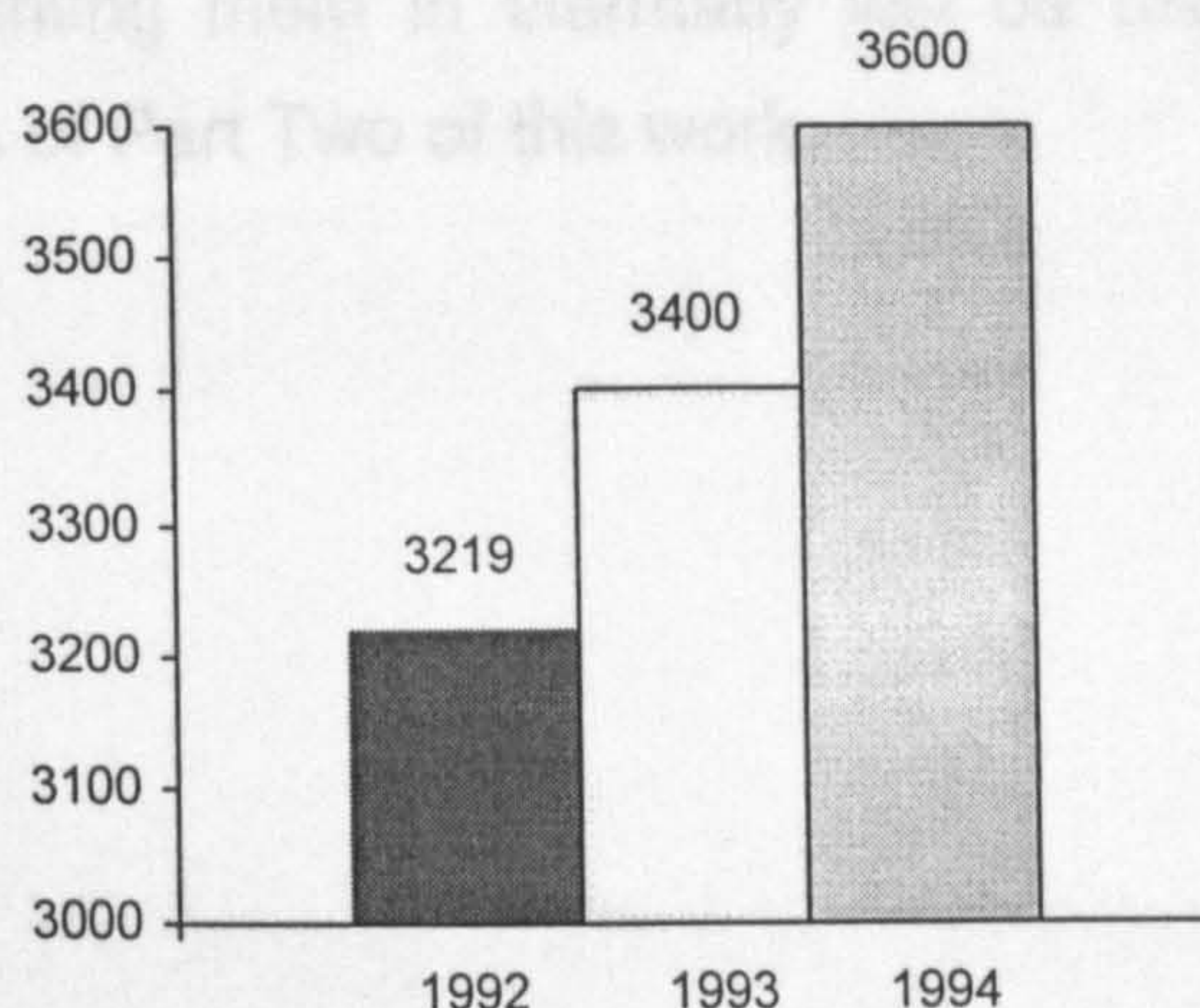
17 AG-Report 1993, R 64.

18 "Gesetz für kleine Aktiengesellschaften und zur Deregulierung des Aktienrechts" vom 2. August 1994 (BGBl. I 1994, S. 1961). See also *Deutscher Bundestag*, Drucksache 12/6721.

19 Sec. 76 VI Betriebsverfassungsgesetz (BetrVG 1952). For details see Chapter 4.2.2.(2)(b) at page 138.

20 For further details see *Kindler*, Die Aktiengesellschaft für den Mittelstand, NJW 1994, 3041.

Table 6: Increase of Stock Corporations
in Germany²¹



To sum up, bearing in mind that the U.K.'s *domestic listed Plc's* outnumber their German equivalent by about 1.100, it is obvious that the British stock-market environment is more favourable for takeover bid activity than the relatively underdeveloped German stock-market. However, the higher number of public companies alone does not explain why takeovers bids are so common in Britain whereas in Germany hostile bids are almost unknown.²² Given the high number of privately negotiated acquisitions within Germany both by German and European companies shown in Table 1 at page 18, it can be ruled out that the virtual non-existence of takeover bids in Germany

21 Source: *AG-Report* 1995, R 272.

22 For an empirical study see *Wymeersch*, Unternehmensführung in Westeuropa, AG 1995, 299, 307. Also *Krause*, Zur Gleichbehandlung der Aktionäre bei Übernahmeangeboten und Beteiligungserwerb WM 1996, 845; *Neye*, Der neue Übernahmekodex, ZIP 1995, 1464; *Thoma*, Der neue Übernahmekodex der Börsensachverständigenkommission, Osnabrück, Arbeitspapier 9/96, p. 4.

is due to lack of economic interest. In fact, more (privately agreed) cross-border acquisitions by Community companies were made in Germany (642) than in Britain (408). The reasons for the absence of a lively public bid activity, the alleged lack of a level playing field, therefore must have deeper rooted legal and maybe (business-) cultural reasons. The legal environment encouraging takeover bids in Britain and preventing them in Germany will be discussed in the following chapters of Part Two of this work.

PART TWO

Takeover Regulation and Barriers

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Chapter 3

Takeover Regulation and Barriers in Britain

In order to explain the rather opposite takeover situation in the U.K. and Germany, Chapter 3 begins with a description and analysis of the legal takeover environment in Britain. More specifically, Chapter 3.1 looks at the regulatory framework in the U.K. Chapter 3.2 continues with a study of the existing structural barriers to takeovers and, finally, Chapter 3.3 examines the defences open to the directors of a target company. The German side will be explored in a similarly structured chapter in Chapter 4.

3.1. The Regulatory Framework

The regulatory framework governing acquisitions of listed public companies consists of a complex mix of statutory and non-statutory rules.¹ Whereas the legal provisions contained in the Companies Act 1985 and the Financial Services Act 1986 cover only few aspects of takeover bids, the vast majority of the regulation is to be found in the self-regulatory rules of the "*City Code on Takeovers and Mergers*",² the "*Rules Governing Substantial Acquisitions of Shares*",³ and the

1 *Begg, Corporate Acquisitions and Mergers*, para 2.01 describes the situation graphically as being "*somewhat like a zoo.*"

2 Hereafter the City Code.

3 Hereafter the SARs.

Stock Exchange's rules entitled "*The Listing Rules of the Stock Exchange*", the latter being generally referred to as the "*Yellow Book*".⁴ Self-regulation therefore is a most characteristic feature of the British regulation of takeovers.⁵ Although this structural concept is widely treasured,⁶ it is not beyond criticism.⁷ The pros and cons of self-regulation will be considered in Chapter 5 in connection with the proposed EC-Directive on Takeovers and Mergers.⁸

The competition aspects of takeovers are exclusively controlled by the Fair Trading Act 1973⁹ and on European level most notably the Merger Control Regulation 4064/89.¹⁰

3.1.1. The City Code on Takeovers and Mergers

The origins of the Code go back to 1959 when after a spectacular takeover battle¹¹ a body known as "*The City Working*

4 The so called "*Green Book*" of the Stock Exchange regulates the Unlisted Securities Market (USM), where about 200 companies are registered, which is going to be phased out at the end of 1996. The USM is succeeded by the Alternative Investment Market (AIM) which was opened in June 1995. As to these developments see *Times*, 16 February 1995 and 31 July 1995; *Editorial*, (1995) B.L.R., Vol. 16. p. 2, 15; *Financial Times*, 17 May 1996: as of May 1996 there were 140 companies listed on AIM.

5 R. v. Panel on Takeovers and Mergers, ex parte Datafin Plc. [1987] QB 815, 824-826; concerning the general concept of self-regulation in the field of company law see Bovey, Self-Regulation, Company Lawyer, Vol. 12, No. 1, p. 3 (1991); see also Morse, The City Code on Takeovers and Merger - Self Regulation of Self Protection?, [1991] J.B.L. 509; Lord Alexander of Weedon, Takeovers: The Regulatory Scene, [1990] J.B.L. 203.

6 As to the merits of self-regulation see e.g. Lord Alexander of Weedon, Takeovers: The Regulatory Scene, [1990] J.B.L. 203.

7 Critical of the concept of self-regulation e.g. Jowell, The Takeover Panel: Autonomy, Flexibility and Legality, [1991] P.L. 149.

8 See Chapter 5.1.1.(1) at p. 175 and Chapter 5.1.2.(1)(a) at p. 181.

9 See Chapter 6, p. 265 -334.

10 See Chapter 8, p. 335-389.

11 Involving the U.S. companies *Reynolds Metals* and *Aluminium Corporation of America* as rival bidders for *British Aluminium*, see Johnston, Takeover Code, p. 14-16.

Party" was established by leading City institutions¹² at the instigation of the Bank of England.¹³ Their duty was to examine good business practice in the conduct of takeovers and mergers in order to prevent parliamentary legislation in this field. In 1959 the "*Notes on Amalgamations of British Business*" were proclaimed.¹⁴ Nine years later the growing extent of fierce takeover battles made it necessary to form a new set of rules, and in 1968 the City Working Party published the first edition of the Code. In the same year the Panel on Takeovers and Mergers¹⁵ was set up on the initiative of the Governor of the Bank of England to monitor takeovers and mergers. Since that time the Code is issued and administered by the Panel. The fourth and latest edition was published on July 8, 1993.¹⁶

(1) Scope and Structure

The main function of the Code is to ensure a fair and equal treatment of all shareholders in relation to takeovers and to provide a regulatory framework for the conduct of takeovers. The Code is supposed to represent the collective opinion of those professionally involved in the field of takeovers as to good business standards and as to how fairness to shareholders can be achieved.¹⁷ The Code is, however, not concerned with competition policy¹⁸ and is also not

12 The Accepting Houses Committee, the Association of Investment Trust Companies, the Association of Unit Trust Managers, the British Insurance Association, the Committee of London Clearing Bankers, the Confederation of British Industry, the Issuing Houses Association, the National Association of Pension Funds, and the London Stock Exchange.

13 As to the history of the City Code and the Panel see *Johnston*, Takeover Code, p. 9; Halsbury's Laws of England, Vol. 7 (1) para 1035; *Begg*, Corporate Acquisitions and Mergers, para 9.59.

14 *De Montmorency*, Takeover Bids, [1963] J.B.L. 246, 249.

15 Hereafter the Panel. See in detail Chapter 3.1.2. at p. 36 et seq.

16 Reproduced in *Palmer's Company Law*, 25th edition, Vol. 2, Part D.

17 The City Code, Introduction, para 1 (a).

18 Although the Code provides in Rule 12 for the possibility of a merger reference to the Monopolies and Mergers Commission or the European Commission.

concerned with the merits of a particular takeover bid.¹⁹ Whereas the former question is left to the government and the EC-Commission the latter is ultimately to be decided upon by the shareholders of the target company.

As to the scope of the Code, it is principally applicable to all offers for listed and unlisted public companies resident in the United Kingdom, the Channel Islands or the Isle of Man.²⁰ The nature of the offeror company is in contrast of no importance in determining whether the Code applies or not.²¹ The Code does not apply to offers for non-voting non-equity capital.²²

The Code is divided into 18 chapters (A to Q), including an introduction, and contains three different categories of provisions. First, there are 10 *General Principles* which form a basic outline of the good business standard the Code seeks to ensure. The General Principles are followed by 38 *Rules*.²³ The Rules are subdivided into many subsections and further supplemented by *Notes*. Moreover, the Code is complemented by 4 Appendices.²⁴ The Rules are partly of a procedural nature and designed to govern specific types of takeovers and partly represent mere examples for the application of the General Principles. The Notes provide guidelines for the application of the Rules. Because of the Code's non-statutory nature and its purpose to be a rule of conduct for the business community,

19 The City Code, Introduction, para 1 (a).

20 The Code also applies to all offers for companies considered by the Panel to be resident in the Irish Republic if their shares are listed on The Stock Exchange or dealt in on the Unlisted Securities Market, see The City Code, Introduction, para 4 (a).

21 The City Code, Introduction, para 4 (a). Only in certain limited cases (specified in the Introduction, para 4) offers for private companies are subject to the City Code.

22 The City Code, Introduction, para 4 (b).

23 The first edition of the Code in 1968 already embodied 35 Rules.

24 Appendix 1: Whitewash Guidance Note.

Appendix 2: Formula Offers Guidance Note.

Appendix 3: Directors' Responsibilities and Conflicts of Interest Guidance Note.

Appendix 4: Receiving Agents' Code of Practice.

the language is rather simple and non-technical.²⁵ According to the Code, persons involved in an offer have to observe the spirit as well as the precise wording of the General Principles and the pertaining Rules. As a result of this purposive or teleological approach, the rules can be waived in favour of underlying principles.²⁶ Additionally, the General Principles and the spirit of the Code are to be considered where the circumstances of the particular case are not explicitly covered by any Rule.²⁷ Thus, it is the spirit and purpose of the Code, and not its letter, that ultimately prevails.

(2) Fundamental Principles underlying the Code

The fundamental principles underlying the Code as a whole may be condensed to the following four basic maxims:²⁸

(a) Equality of Treatment

This tenet is not only expressed in General Principle 1, but also reflected in numerous rules. One example is Rule 6 which provides that where the offeror has purchased shares at above the offer price during the offer period then that offer must be increased accordingly for the benefit of the remaining shareholders. Another example for the equality of treatment is the requirement of a mandatory offer to all shareholders in Rule 9 when a person acquires 30 per cent or

25 The City Code, Introduction, para 3 (a); *Begg*, Corporate Acquisitions and Mergers, para 9.64.

26 *Calcutt*, The Work of the Takeover Panel, Company Lawyer, Vol. 11, No. 11, p. 203, 205 (1990); *Jowell*, The Takeover Panel: Autonomy, Flexibility and Legality, [1991] P.L. 149, 151.

27 The City Code, Introduction to the General Principles.

28 *Calcutt*, The Work of the Takeover Panel, Company Lawyer, Vol. 11, No. 11, p. 203, 205 (1990); *Jowell*, The Takeover Panel: Autonomy, Flexibility and Legality, [1991] P.L. 149, 151; *Lord Alexander of Weedon*, Takeovers: The Regulatory Scene, [1990] J.B.L. 203, 204, 205.

more of the voting rights. This offer must be at the highest price paid by him in the previous 12 months and be in cash or include a cash alternative. By this means, the Code prevents the acquirer from getting effective control of the target company without giving the remaining minority a chance to participate in the premium paid for the control. A last illustration of the principle of fair treatment is Rule 11. Rule 11 affects the consideration of a voluntary offer. When during the offer period or within 12 months prior to the commencement of the offer period the offeror purchases 10 per cent or more of the voting shares for cash, the offer must include a cash alternative for all the shares of that class at the highest price paid by the offeror during the relevant period.²⁹ In that way the offeror is precluded from paying more important shareholders a special cash price while the others get a somewhat less attractive share for share deal.

(b) Adequate Information

Another fundamental element of the Code, which is contained in General Principle 4 and Rule 23 and various other Rules, is the provision of adequate information to shareholders in sufficient time to enable them to consider the merits of the offer and reach a properly informed decision. Rule 20 requiring equality of information for all shareholders restricts, for example, press, television and radio

29 The most spectacular case concerning a breach of Rule 11 is the takeover of Distillers by Guinness: *R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc.* [1989] 1 All ER 509. Acting secretly in concert with a swiss company, Guinness purchased more than the then allowed 15 per cent of the shares in Distillers for cash. Consequently, Guinness had to pay the difference between the offer price and the highest paid cash price to all Distillers' shareholders - a sum which amounted to £85.000.000. As to the calculation of that amount see *Morse, The City Code on Takeovers and Mergers - Self-regulation or Self-Protection* [1991] J.B.L. 509, 521.

interviews during the offer period,³⁰ and Rule 24 provides for detailed information in the offer document itself.

(c) Transparency in Dealings

Instead of prohibiting further dealings during the offer period, trading in the shares of the offeror company and the target company will normally continue. However, the Code seeks to ensure a fair market by requiring strict transparency of dealings. In principle, during the offer period the offeror, the offeree company, and any associates must disclose any dealings in the relevant securities of the offeror³¹ and the target company publicly, namely to the Stock Exchange, the Panel and the press,³² on the business day following the date of the transaction.³³ The same applies to any other person, whether or not an associate, who owns or controls one per cent or more in a company involved in a takeover.³⁴ In addition to the requirements of the Code, the provisions of the Companies Act 1985 concerning the disclosure of interests in shares apply too.³⁵ But since the obligation of disclosure under the Companies Act 1985 arises only if a person has an interest in shares of three per cent or more,³⁶ it is very likely that, where disclosure is required under the provisions of the Companies Act 1985, disclosure will, if dealing occurs during the offer period, anyway be necessary under Rule 8.3 of the Code, where only one per cent is sufficient to trigger the disclosure requirement.³⁷

30 See Note 1 on Rule 20.1.

31 Dealings in shares of the offeror company must only be disclosed in the case of an securities exchange offer, see Rule 8, NB. 1.

32 Rule 8, Note 4 (a).

33 Rule 8, Note 3.

34 Rule 8.3.

35 Part VI, sections 198-220 CA 1985.

36 Section 199 CA 1985.

37 Rule 8, Note 13.

(d) Restrictions on Frustrating Action

As the United States experience shows,³⁸ where the management of a target company is able to exercise any kind of defence tactics, it is often difficult for the entrenched managers to differentiate between their own interests and those of the shareholders. General Principle 9 therefore states that the directors must always act in their capacity as directors and not have regard to their personal or family shareholdings or to their personal relationship with the company. In accordance with this understanding, General Principle 7, which is further specified in Rule 21, provides that the management of the target company has no right to take any action, except with the consent of the shareholders, which could effectively result in any bona fide offer being frustrated and consequently in the shareholders being denied the opportunity to decide on the merits of a bid. Instead, under Rule 3.1 the board of the target company has to seek independent advice and the substance of the advice must be made known to the shareholders. Under Rule 19.4 the offeree management is even required to give equal information to competing bidders in order to prevent any undue preference to the suitor favoured by the target's management. The question whether, and if so which, defensive action can be taken in spite of General Principle 7, namely in advance of a bid or with the consent of the shareholders will be considered in Chapters 3.3.³⁹ and 3.4.⁴⁰

38 *Solomon/Schwartz/Baumann, Corporations*, p. 1031, 1143.

39 See p. 70 et seq.

40 See p. 85 et seq.

3.1.2. The Takeover Panel

The former Master of the Rolls, *Lord Donaldson*, introduced his judgement in the famous *Datafin* case by describing the Panel as a "*truly remarkable body*" which, "*perched on the 20th floor of the Stock Exchange building in London, both literally and metaphorically oversees and regulates a very important part of the United Kingdom financial market.*"⁴¹

As part of the self-regulatory system the Panel has no statutory power at all and is not in any contractual relationship with the financial market or those who deal in the market.⁴² Legally, the Panel is an unincorporated association with legal personality.⁴³

(1) Structure of the Panel

Analysing the structure of the Panel, it is to differentiate between the main membership body, the so called full Panel, the Executive and the Appeal Committee.⁴⁴

The day-to-day work of the Panel is carried out by the Executive, which is working full-time.⁴⁵ Its workload is considerable as Table 9 (first column) at page 41 shows. The Executive consists of a Director General,⁴⁶ who is usually a senior merchant banker experienced in corporate finance, three Deputy Directors-General,⁴⁷ two

41 R. v. Panel on Takeovers and Mergers, ex parte *Datafin Plc.* [1987] QB 815, 824.

42 Ibid, p. 825.

43 Ibid, p. 824.

44 An up to date list of all members of the Panel, the Appeal Committee, and Executive is contained in the annual reports of the Panel.

45 The City Code, Introduction, para 2 (b).

46 As at 18 July 1996 these was Alistair N C Defriez, seconded from SBC Warburg.

47 As at 18 July 1996 these were *T Peter Lee*, *Noel P Hinton*, and *Anthony G B Pullinger*.

Secretaries,⁴⁸ eight Assistant Secretaries⁴⁹ and supporting staff of about 16 people, some of whom are on secondment and some are permanent staff, with backgrounds in the Bank of England, merchant banks, the Stock Exchange, accountancy and solicitors' firms, and other City institutions.⁵⁰ The mixture of permanent staff and others on secondment guarantees a wide range of experience represented in the Executive and is thus beneficial for the Executive's quality of work.⁵¹

In contrast to the Executive, the full Panel meets only occasionally to hear any matters referred to it by the Executive⁵², appeals by parties from the Executive's decisions, and disciplinary matters.⁵³ In the year to 31 March 1995, for example, which was a relatively busy year for the full Panel, it held six meetings to hear appeals against rulings by the Executive.⁵⁴ As Table 9 at page 41 indicates, only a relatively small percentage of appeals made to the full Panel are successful. To be precise, from the year ended 31 March 1989 to 31 March 1996 a total of 33 appeals were made to the Panel of which only three were fortunate.

48 As at 18 July 1996 these were *Carlton P Evans* (Linklaters & Paines) and *Michael D Shaw* (Herbert Smith).

49 As at 18 July 1996 these were *Helena R M Z Skarbek* (Bank of England), *Leonie S Grimes* (Arthur Anderson), *Richard Ozsanlav* (Coopers & Lybrand), *Angus W Pottinger* (Merrill Lynch), *Edward J M Baker* (Ashurst Morris Crisp), *Bernadette M McKernan* (Deloitte & Touche), *Patrick J Magee* (J P Morgan), *Jane M Taylor*. All but *Jane Taylor* are seconded.

50 See previous footnote. Also *R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc.* [1989] 1 All ER 509, 514; *Calcutt*, *The work of the Takeover Panel*, *Company Lawyer*, Vol. 11, No. 11, p. 203 (1990). Concerning the Panel's composition and staffing see also *The Trade and Industry Committee Report on Takeovers and Mergers*, 1991, para 135 et seq.

51 *Calcutt*, *The work of the Takeover Panel*, *Company Lawyer*, Vol. 11, No. 11, p. 203 (1990).

52 The City Code, Introduction, para 1 (b). In 1990-91 seven meetings were held, three of which were on appeals from parties to bids and one on a disciplinary matter. See *The Trade and Industry Committee Report on Takeovers and Mergers*, 1991, para 135.

53 The City Code, Introduction, para 1 (c).

54 The Takeover Panel, 1994-1995 Report, p. 15.

The actual membership of the Panel comprises a Chairman,⁵⁵ two Deputy Chairmen⁵⁶ and three independent members, each appointed by the Governor of the Bank of England.⁵⁷ In addition, there are 12 members, who represent various City organisations as Table 7 at page 39 shows. The composition of the Panel is designed to comprehend all those who are professionally involved in takeovers. There has been criticism that the Panel looks excessively biased towards those with a direct financial interest in creating more takeover activity.⁵⁸ Table 7 at page 39 demonstrates that point impressively. Trade unions, for example, are not represented. Both the members of the Panel and the Executive almost exclusively come from a financial background in a major City institution. The 1994/1995 Director General of the Executive, for instance, *William Staple*, who is the brother of the director of the Serious Fraud Office, *George Staple*, was on a two-year secondment from the investment bank *N.M. Rothschild*.⁵⁹ The present Director General,⁶⁰ *Alistair Defriez*, is seconded from *SBC Warburg*. Surely, given the composition of the Panel and the Executive there seems to be a potential for conflicts of interest. This problem is to some extent inherent in the concept of *self-regulation* where those who devise the rules draw them up in their own interest to avoid government legislation which might not be as flexible and favourable.

55 As at 18 July 1996 this was *Sir David Calcutt* QC, former Chairman of the Bar.

56 As at 18 July 1996 these were *John F C Hull*, former Chairman of J Henry Schroder Wagg & Co and *John F Goble*, former Senior Partner Herbert Smith.

57 The City Code, Introduction, para 2 (a); *Calcutt*, The work of the Takeover Panel, Company Lawyer, Vol. 11, No. 11, p. 203 (1990).

58 *Jowell*, Self-regulation under threat, *Financial Times*, May 9, 1991.; see also The Trade and Industry Committee Report on Takeovers and Mergers, 1991, para 135 et seq.

59 Since March 1994. *Financial Times*, January 8, 1994.

60 As at 18 July 1996.

Table 7: Background of Panel Members 1996

Name	Function - Representative of	Position
Sir David Calcutt QC	Panel Chairman appointed by Bank of England	Former Chairman of the Bar
John F Hull	Panel Deputy Chairman appointed by Bank of England	Former Chairman, J Henry Schroder Wagg & Co
John F Goble	Panel Deputy Chairman appointed by Bank of England	Former Senior Partner, Herber Smith
Sir Christopher Benson	Independent Member appointed by Bank of England	Chairman, Sun Alliance Group
H Dennis Stevenson	Independent Member appointed by Bank of England	Chairman, SRU
Robert B Jack	Independent Member appointed by Bank of England	Former Senior Partner, McGrigor Donald
John G T Carter	Chairman, Association of British Insurers	Chief Executive, Commercial Union
Douglas C P McDougall	Chairman, Association of Investment Trust Companies	Joint Senior Partner, Baillie Gifford & Company
Clive N Boothman	Chairman, Association of Unit Trusts and Investment Funds	Managing Director, Schroder Unit Trusts
Sir Brian Pitman	President British Bankers' Association	Group Chief Executive, Lloyds TSB Group
Martin F Broughton	Nominated by Confederation of British Industry	Group Chief Executive, BAT Industries
Brian M Currie	President, Institute of Chartered Accountants in England and Wales	Former Managing Partner, Arthur Anderson, London
Charles K R Nunneley	Chairman, Investment Management Regulatory Organisation	Deputy Chairman, Robert Fleming Holdings
John L Walker-Haworth	Nominated by London Investment Banking Association	Managing Director, SBC Warburg
Antony R Beevor	Chairman, London Investment Banking Association Corporate Finance Committee	Executive Director, Hambros Bank
John Kemp-Welch	Chairman, London Stock Exchange	Former Senior Partner Cazenove & Co
Graham K Allen	Nominated by National Association of Pension Funds	Managing Director, ICI Investment Management
Nicholas J Durlacher	Chairman Securities and Futures Authority	Director, Barclays De Zoete Wedd Securities

Source: 1995-1996 Report of the Takeover Panel

Table 8: Background of Executive Members 1996

Name	Function	Seconded from
Alistair N C Defriez	Director General	SBC Warburg
T Peter Lee	Deputy Director General	--
Noel P Hinton	Deputy Director General	--
Anthony G B Pullinger	Deputy Director General	--
Carlton P Evans	Secretary	Linklaters & Paines
Michael D Shaw	Secretary	Herbert Smith
Helena R M Z Skarbek	Assistent Secretary	Bank of England
Leonie S Grimes	Assistent Secretary	Arthur Anderson
Richard Ozsanlav	Assistent Secretary	Coopers & Lybrand
Angus W Pottinger	Assistent Secretary	Merrill Lynch
Edward J M Baker	Assistent Secretary	Ashurst Morris Crisp
Bernadette M McKernan	Assistent Secretary	Deloitte & Touche
Patrick J Magee	Assistent Secretary	J P Morgan
Jane M Taylor	Assistent to the Secretary	--

Source: 1995-1996 Report of the Takeover Panel

The Appeal Committee hears appeals from the Panel’s decisions. It is headed by a Chairman and a Deputy Chairman who will normally have held high judicial office.⁶¹ The Chairman sits with two members of the Panel who were not involved in the Panel’s decision under appeal. The right of appeal is granted only in certain cases, in particular where the Panel proposes to take disciplinary action or it is alleged that the Panel has acted outside its jurisdiction (see Table 9 at page 41). But an appeal may in all cases be made to the Appeal Committee with leave of the Panel.⁶² However, leave will not normally be granted on findings of fact or interpretation of the

61 As at 18 July 1996 these were the *Rt Hon Sir Michael Kerr*, former Lord Justice of Appeal, and the *Rt Hon Sir Christopher Slade*, former Lord Justice of Appeal.

62 For further details see The City Code, Introduction, para 3 (f).

Code.⁶³ As Table 9 (last column) at page 41 shows, the role of the Appeal Committee is very limited indeed. From 1989 until 31 March 1996 there have only been seven appeals to the Appeal Committee, none of which was successful.

Table 9: Panel Workload

Year ended 31 March	Published Takeover Proposals	Full Panel Meetings	Cases referred to the Panel by the Executive	Appeals to the Panel by parties (successful)	Disciplinary Cases	Appeals to the Appeal Committee (successful)
1989	253	14	3	8 (-)	2	1 (-)
1990	230	13	5	6 (2)	1	3 (-)
1991	132	7	3	3 (-)	1	- (-)
1992	142	5	1	2 (-)	2	2 (-)
1993	88	6	-	5 (-)	1	- (-)
1994	81	1	-	1 (-)	-	- (-)
1995	108	6	-	6 (1)	-	1 (-)
1996	156	2	-	2 (-)	-	- (-)

Source: Annual Reports of the Takeover Panel

(2) Functions of the Panel

The Panel has often been described as the whistle-blowing referee of the fair conduct of a bid.⁶⁴ Yet, that is only part of its functions⁶⁵ which are basically fourfold.⁶⁶

⁶³ The City Code, Introduction, para 3 (f); see also *Morse*, Role of the Panel's Appeal Committee defined, [1990] J.B.L. 67, 69.

⁶⁴ *R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc.* [1989] 1 All ER 509, 511; *Lord Alexander of Weedon*, Takeovers: The Regulatory Scene, [1990] J.B.L. 203, 204.

First of all, the Panel is the *legislator* of the Code. Its second function is to act as an *interpreter* of it, and thirdly, the Panel is concerned to *monitor compliance* with the Code and to investigate alleged breaches.⁶⁷ To strengthen its investigative powers, the Panel became a designated authority⁶⁸ under the Companies Act 1985,⁶⁹ the Financial Services Act 1986,⁷⁰ and the Banking Act 1987. It is for that reason entitled to receive information obtained under those Acts which is otherwise not publicly available. Last but not least, the fourth function of the Panel is to *impose sanctions* to enforce the Code; it acts thus as a disciplinary tribunal.⁷¹

The Panel is, hence, much more than a mere referee. Other than a referee, the Panel makes the rules it interprets and even has the power to waive the Code's written rules in favour of the spirit of the Code.⁷² Apart from the possibility of judicial review of the Panel's decisions, which is rather limited in its practical effect,⁷³ there is no separation of power at all.

Whereas a referee is usually subject to the public scrutiny of the crowds, the Panel acts more or less behind closed doors, and the hearings before the Panel are - for the sake of speediness and effectiveness - informal and private.⁷⁴ There are no rules of

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- 65 Jowell, The Takeover Panel: Autonomy, Flexibility and Legality, [1991] P.L. 149, 150.
 - 66 R. v. Panel on Takeovers and Mergers, ex parte Datafin Plc. [1987] QB 815, 841.
 - 67 As to the relative weakness of the Panel's investigative powers see Morse, The City Code on Takeovers and Mergers - Self-regulation or Self-Protection, [1991] J.B.L. 509, 515-519.
 - 68 S.I. 1987 No. 859.
 - 69 Sections 447, 449 (3) CA 1985: information acquired by the DTI under "books and papers" inspections.
 - 70 Sections 179, 180 Financial Services Act 1986: entitled to receive otherwise restricted information.
 - 71 R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc [1989] 1 All ER 509, 511. See Chapter 3.1.2. (3) at pp. 44.
 - 72 See Chapter 3.1.2.(1) at pp. 36.
 - 73 See Chapter 3.1.2.(4)(b) at pp. 53.
 - 74 The City Code, Introduction, para 3 (e); for a thorough description of the Panel's procedure see R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc. [1989] 1 All ER 509, 515.

evidence, and even legal representation at hearings before the Panel is not normally allowed!⁷⁵

Among the four functions of the Panel, the one as interpreter of the Code, or in other words, as a consultant to the persons involved in the takeover bid, is the most important one from a practical point of view. When there is any doubt whether a proposed course of conduct in a takeover bid is in accordance with the Code, parties and their advisers are strongly encouraged to consult the Executive either in advance or at any time during the course of the bid.⁷⁶ During the offer period the Panel Executive is usually in daily contact with the parties' advisers, and the Executive's Director General, or one of his Deputies, is constantly available to give rulings on points of interpretation of the Code or for consultation.⁷⁷ Although there has been criticism regarding the institutional self-regulatory framework with its inherent risk of conflict of interest, the quality of the Executive's work as such has to the author's knowledge never really been disputed. This may be one reason why in the vast majority of cases its rulings are simply accepted by the parties and their advisers, and no further reference is made to the full Panel and the Appeal Committee.⁷⁸ Another reason may be, however, that the chance of success appears to be very low indeed as Table 9 at page 41 indicates.

75 Ibid.

76 The City Code, Introduction, para 3 (b); *R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc.* [1989] 1 All ER 509, 514; *Calcutt*, The work of the Takeover Panel, Company Lawyer, Vol. 11, No. 11, p. 204 (1990).

77 *R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc.* [1989] 1 All ER 509, 515.

78 Ibid. According to The *Trade and Industry Committee Report on Takeovers and Mergers*, 1991, para 136 there were only three appeals from parties to bids and one on a disciplinary matter in 1990-91.

(3) Enforcement of the Code

Although the Panel is a self-regulatory body and has no authority *de jure* to enforce the Code, quite a number of sanctions are open to it.⁷⁹ These vary from quiet private warnings to tough disciplinary actions. That the Panel has no legal power does not mean that it is not operating within a legal framework. On the contrary, the work of the Panel is clearly linked to the regulatory structure established under the Financial Services Act 1986; it is tied in statutorily with the work of other financial regulatory bodies like the Securities and Investments Board (SIB),⁸⁰ the various self-regulating organisations (SROs),⁸¹ and the Stock Exchange. In fact, the Panel's main power derives from the backing by these financial institutions as the following examination shows.

(a) Private Warning

In case of a minor inadvertent breach of the Code causing very little or no damage to investors, the Panel may pronounce a private warning to the offending party and its adviser.⁸²

79 The City Code, Introduction, para 1 (c).

80 See section 114 (2) FSA 1986; Rider/Chaikin/Abrams, Guide to the Financial Services Act, para 302-304.

81 See sections 7-14 FSA 1986. Rider/Chaikin/Abrams, Guide to the Financial Services Act, para 306-311; Begg, Corporate Acquisitions, para 9.04. The four recognised SROs include the following: SFA: The Securities and Futures Association. FIMBRA: The Financial Intermediaries, Managers and Brokers Regulatory Association.

IMRO: The Investment Management Regulatory Organisation. LAUTRO: The Life Assurance and Unit Trust Regulatory Organisation.

82 Begg, Corporate Acquisitions and Mergers, para 9.63; Morse, Self-regulation or Self-protection, [1991] J.B.L. 509, 520.

(b) Public Reprimand

In a more serious case of a breach of the Code, the Panel may issue a public reprimand as a deterrent and sanction. A public reprimand by the Panel may be embarrassing to the advising merchant bank and damage its reputation. It may also lead to some internal disciplinary action within the bank concerned. Surprisingly, there is hardly any of the prominent expert merchant banks which has not been subject to a public reprimand by the Panel for often very patent breaches.⁸³ A recent example is *Rentokil's* £2.2 hostile takeover bid for *BET*, the business services group. The Panel criticised publicly that the defending *BET* management compared in a statement the offer price which did not include dividends with *BET* shares which did include dividend payments which was misleading to *BET* shareholders.⁸⁴

83 See for example: Petrocon Group plc./James Wilkes plc. (Panel Statement February 6, 1992), [1992] J.B.L. 428: breach of Rule 2.2 by Henry Cooke Corporate Finance Ltd., Smith New Court Corporate Finance Ltd., and Rothschild and Sons Ltd.; European Leisure plc./Midsummer Leisure plc. (Panel Statement, May 15, 1990), [1991] J.B.L. 66: breach of Rule 19.3 by Schroder Wagg & Co. Ltd.; Timpson plc./Automagic Holdings plc. (Panel Statement, May 8, 1990), [1991] J.B.L. 65: breach of Rules 1 and 3 of the SARs by Henry Cooke Corporate Finance Ltd.; Meat Trade Supplies plc./Twigrealm plc. (Panel Statement, October 6, 1989), [1990] J.B.L. 73: breach of General Principle 3 by Lloyds Merchant Bank Ltd.; Bowater Industries plc./Norton Opax plc./The De La Rue Co. plc. (Panel Statement, September 11, 1989), [1990] J.B.L. 73: breach of Rule 19.3 by Samuel Montagu & Co. Ltd.; Franke Holdings AG/Carron Phoenix plc. (Panel Statement, January 25, 1990), [1990] J.B.L. 337: breach of Rule 6.2 (2) by *Brown*, Shipley & Co. Ltd.; DRG plc. (Panel Statement, November 3, 1989), [1990] J.B.L. 33: breach of Rule 19 by Lazard Brothers & Co. Ltd.; Electronic Data Systems Corporation/SD-Scicon plc. (Panel Statement, August 21, 1991) [1992] J.B.L. 105: breach of note 3 on Rule 20.1 by Samuel Montague & Co. Ltd.

84 *Financial Times*, 13/14 April 1996.

(c) Remedial Measures

If there has been damage to investors or the other side, the Panel may require the offending party to take remedial action such as to make the required mandatory offer,⁸⁵ to pay compensation to prejudiced investors,⁸⁶ to issue an amended circular,⁸⁷ to dispose of the shares acquired in breach of the Code,⁸⁸ or not to vote with the shares purchased in violation of the Code.⁸⁹ However, if the offending party refuses to act accordingly, the Panel itself has no direct means to force the offending party to comply with its ruling. To reach this goal, the Panel needs the support of the self-regulating organisations (SROs) established under the Financial Services Act 1986 and the Stock Exchange. The way this works is dealt with in the following paras.

(d) Sanctions against advisers through the SROs

Under the Financial Services Act 1986 no person has the right to carry on investment business, which includes takeover activity, unless he is authorised to do so.⁹⁰ In broad outline, authorisation is generally obtained through membership of a recognised SRO.⁹¹ Recognition is conferred on the SROs by the Securities and

85 Gasco Investments Ltd./St. Piran Ltd., [1980] J.B.L. 270, 358.

86 Guinness plc./The Distillers Company plc. (Panel Statement, July 14, 1989), [1989] J.B.L. 520: Guinness had to pay £85m in compensation to Distillers' shareholders.

87 Meat Trade Supplies plc./Twigrealm plc. (Panel Statement, October 6, 1989), [1990] J.B.L. 73.

88 Timpson plc./Automagic Holdings plc. (Panel Statement, May 8, 1990), [1991] J.B.L. 65.

89 Crest International Securities Ltd./Ashbourne Investments Ltd., [1975] J.B.L. 44.

90 Section 3 FSA 1986. As to investment advertisements (offer document) see section 57 FSA 1986.

91 Section 7 FSA 1986.

Investments Board (SIB)⁹² to which the functions of the Secretary of State are delegated.⁹³ Practically all merchant banks or other advisers involved in takeover activity are members of a SRO, most probably the SFA⁹⁴ or FIMBRA.⁹⁵ The SROs are defined as bodies regulating the carrying on of investment business by enforcing rules which are strictly binding on their members.⁹⁶ Contrary to the Panel, the SROs' rules and constitution must meet clearly defined statutory criteria outlined in the Financial Services Act and put into more concrete terms by the SIB's "*Conduct of Business Rules*."⁹⁷ Under these rules, failure to adhere to the Code calls into question a firm's status as a "fit and proper" investment business.⁹⁸ In this kind of situation a variety of sanctions are open to the relevant SRO.⁹⁹ Ultimately, disciplinary actions can lead to the suspension or even revocation of authorisation, which means the respective merchant bank is then by virtue of section 3 of the Financial Services Act 1986 temporarily or permanently restricted from carrying on any investment business. The available sanctions against merchant banks acting in breach of the Code are thus very powerful. But the question is whether these sanctions are applied strictly against offending merchant banks, which is only possible if the Panel refers breaches of the Code to the relevant SRO. In most cases, however, the Panel simply criticises the offending merchant bank for the breach,¹⁰⁰ whereas sanctions against offending parties sometimes

92 The SIB is a private company limited by guarantee. The exercise of the SIB's statutory powers is subject of judicial review.

93 Sections 10, 114 FSA 1986; note also the Transfer of Functions Order 1992 - S.I. 1992/1315 which refers certain functions from the Secretary of State to the Treasury.

94 The Securities and Futures Association.

95 The Financial Intermediaries, Managers and Brokers Regulatory Association.

96 Section 8 (1) FSA 1986.

97 See sections 48, 114 and Schedule 8 of the FSA 1986.

98 *Gore-Browne* on Companies, para 29.2.3.; *Begg*, Corporate Acquisitions and Mergers, para 9.57.

99 *Rider/Chaikin/Abrams*, Guide to the Financial Services Act, para 1207-1213.

100 See Chapter 3.1.2.(3)(b) at pp 45.

seem rather harsh.¹⁰¹ Accordingly, there has been suspicion that in connection with breaches of the Code the Panel pursues offeror and offeree boards more vigorously than their advisers,¹⁰² and that *"nothing will happen if you are part of the charmed circle"* of merchant banks.¹⁰³ It has also been asked whether the Panel *"is concerned with the full enforcement of the Code or is conducting a damage limitation exercise for the City."*¹⁰⁴

(e) "Cold-Shouldering"

Whereas the advisers to a takeover party run the considerable risk of losing their authorisation to carry on investment business if they breach the Code, it has been a slightly more difficult task to impose effective sanctions upon the companies concerned and their directors. The *Ashbourne*¹⁰⁵ and *St. Piran*¹⁰⁶ sagas of the early 1980s are infamous examples of the fact that the Panel's authority has not always been accepted. However, this seems to have changed as the case of *Guinness*, where the company was forced to pay £85.000.000 to Distillers' shareholders, shows.¹⁰⁷ As a result of discussions between the Panel, the DTI, and the SIB in the aftermath of the Guinness-affair, the rules of the SIB and the SROs

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- 101 Compare e.g. *Petrocon Group plc./James Wilkes plc.* (Panel Statement, February 6, 1992), [1992] J.B.L. 428 to *Re Dundee Football Club plc.* (Panel Statement, March 11, 1992) [1992] J.B.L. 430.
- 102 *Morse*, Self-regulation or self-protection, [1991] J.B.L. 509, 519; *Morse*, Breaking the rules - who bears the blame? [1991] J.B.L. 65, 66; *Morse*, Inability to finance an offer, [1992] J.B.L. 105, 106.
- 103 *Morse*, Failure to make timely announcement of offer negotiations, [1992] J.B.L. 428, 429.
- 104 *Morse*, Enforcing and investigating breaches of the City Code, [1990] J.B.L. 336; *Morse*, Breaking the rules - who bears the blame? [1991] J.B.L. 65, 66.
- 105 [1975] J.B.L. 44.
- 106 [1980] J.B.L. 270, 358; see also *Re St. Piran Ltd.*, [1981] 3 All ER 270.
- 107 *R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc.* [1989] 1 All ER 509, 515; see also *Guinness plc./The Distillers Company plc.* (Panel Statement, July 14, 1989), [1989] J.B.L. 520; see also *Morse*, Self-regulation or Self-protection, [1991] J.B.L. 509, 521.

now require authorised investment businesses like merchant banks to decline to act in a takeover for any person who does not appear likely to comply with the Code.¹⁰⁸ Such persons are to be cold-shouldered. In *Re Dundee Football Club Plc*, for example, the key figures, *Mr Drummond* and *Mr Prentice*, acquired secretly acting in concert through various companies far more than 30 per cent of the voting shares in *Dundee Football Club plc* deliberately avoiding the obligation under Rule 9.1 of the Code to make a mandatory offer to the remaining shareholders of *Dundee*.¹⁰⁹ Consequently, both men were subject to serious censure by the Panel, and, moreover, the Panel reported its conclusions to the SIB and the relevant SROs¹¹⁰ for appropriate action by them in the light of their cold-shouldering rules. In effect, all those authorised to conduct investment business were prohibited from acting for either *Mr Drummond* or *Mr Prentice* in connection with takeover matters. Similar to the described cold-shouldering procedure by the SIB and the SROs, the Stock Exchange's Yellow Book expresses explicitly its support for the Code and the Rules Governing Substantial Acquisitions of Shares (SARs).¹¹¹ Thus, a breach of the Code can also lead to the withholding of the facilities of the Stock Exchange by the refusal, discontinuance or suspension of listing,¹¹² which was the case in the notorious *St. Piran-affair*.¹¹³ It should be noted, however, that the suspension of listing has the tendency to be more painful to the innocent shareholders, who in that situation cannot dispose of their

108 Rule 2.12 of the SIB's Conduct of Business Rules. See also The City Code, Introduction, para 1 (c); *Begg*, Corporate Acquisitions and Mergers, para 2.16; *Gower's Principles of Modern Company Law*, p. 706.

109 See e.g. *Dundee Football Club plc*. (Panel Statement, March 11, 1992) [1992] J.B.L. 430.

110 Since *Mr Drummond* was a Scottish solicitor his conduct was reported to the relevant Recognised Professional Body (RPB) too. See section 15, 16 CA 1985.

111 Chapter 10 of the Yellow Book: "*The Exchange supports the City Code and the Rules Governing Substantial Acquisitions of Shares published by the Panel on Takeovers and Mergers, but they do not form part of the listing rules.*"

112 Chapter 1 of the Yellow Book; *Begg*, Corporate Acquisitions and Mergers, para 2.16.

113 [1980] J.B.L. 358; see also *Re St. Piran Ltd.*, [1981] 3 All ER 270.

shares, than to the guilty directors or the company itself. Besides, in *St. Piran* even the suspension of listing proved to be ineffective.¹¹⁴

(f) International Implications

To sum up, since the *St. Piran* affair in the late 1970s and early 1980s the Panel has been remarkably able to enforce its rulings upon domestic companies with a variety of effective sanctions open to it. The Panel also claims to apply the Code successfully to foreign bidders¹¹⁵ and, indeed, so far no major case of defiance by a foreign bidder has hit the headlines. However, foreign implications have caused difficulties already. In the *Minocro* bid for *Consolidated Gold Fields* the Panel was concerned with the effect of legal proceedings in New York which allegedly amounted to a forbidden defensive action by *Consolidated Gold Fields*.¹¹⁶ In the bid by *Hoylake Investments Ltd* for *BAT Industries plc*¹¹⁷ the Panel had to consider the impact of procedural requirements in the United States, where *Hoylake* needed to obtain the approval by the insurance commissioners in nine States, upon the bid timetable in the U.K. In the case of *Luric Corp's* bid for *Merlin International Properties Ltd* the Panel stated that the standard of care required under General Principle 3 has an additional dimension where a financial adviser is acting for a newly created off-shore overseas company.¹¹⁸ It remains to be seen, however, whether the self-regulatory system, which depends to a large extent on the mutual respect, co-operation and closeness of the British business community in the City of London, works equally well when seriously challenged by a foreign

114 *Morse*, Self-regulation or Self-protection, [1991] J.B.L. 500, 521.

115 *Bovey*, Self-regulation, *Company Lawyer*, Vol. 12, No. 1, p. 4, (1991); *Calcutt*, The work of the Takeover Panel, *Company Lawyer*, Vol. 11, No. 11, p. 203, 207 (1990).

116 Panel Statement, May 9, 1989, [1989] J.B.L. 427.

117 Panel Statement, September 6, 1989, [1990] J.B.L. 67, 68.

118 Panel Statement, August 12, 1991, [1992] J.B.L. 105, 106.

bidder. Obviously, methods like public censuring and cold-shouldering look less frightful to a foreign offeror company which is not listed on the Stock Exchange, and it is likely that sooner or later the Panel will have to prove its strength at an international stage.

(4) Judicial Review

As discussed above, the Panel operates within a legal framework in so far as it is a designated authority¹¹⁹ to receive otherwise restricted information and is linked to the regulatory system established under the Financial Services Act and the Stock Exchange.¹²⁰ A further respect in which the Panel operates within a legal framework is that it is subject to judicial review as the *Datafin* decision established.¹²¹ Judicial review is basically a process by which the courts¹²² exercise a supervisory jurisdiction over the activities of public authorities in the field of public law.¹²³ In contrast to an appeal, judicial review is neither concerned with evaluating evidence nor is it a fact-finding procedure. The courts do also not review the substantive merits of the public authority's decision in question,¹²⁴ and consequently the Courts do not substitute their own judgement of reasonableness for that of the decision-maker. The grounds on which judicial review can be granted are, broadly speaking, limited to situations where a public body exceeds its

119 See Chapter 3.1.2. (2) at pp. 41.

120 See Chapter 3.1.2. (3)(d) at pp. 46.

121 *R. v. Panel on Takeovers and Mergers, ex parte Datafin Plc.* [1987] QB 815, 824.

122 Usually the High Court. See section 29 (1) of the Supreme Court Act 1991. As to the procedure in detail see Rules of the Supreme Court, Order 53.

123 *McLeod*, Judicial Review, p. 1.

124 *R. v. Panel on Takeovers and Mergers, ex parte Datafin Plc.* [1987] QB 815, 842.

jurisdiction (illegality), acts irrational (irrationality), or against the rules of natural justice (procedural impropriety).¹²⁵

In the *Datafin* case, where *Datafin* challenged the Panel's decision that a rival bidder for *McCorquodale*, *Norton Opax*, was not acting in concert with another company, two questions of fundamental interest arose. First of all, it was unclear whether the Panel as a self-regulatory body could be subject to judicial review (the jurisdictional issue). Of equally great interest was the second question, namely in which way the court would exercise a given jurisdiction to grant judicial review (the practical issue).

(a) The Jurisdictional Issue

Judicial review extended traditionally only to public authorities, i.e. bodies either based on statutory or prerogative power.¹²⁶ The Panel, however, is a self-regulatory organisation which is neither based on statute nor on prerogative authority and, thus, *prima facie* a private body. Nevertheless, various reasons led *Lord Donaldson M.R.* to the conclusion that the Panel, regulating and policing the conduct of takeovers and mergers in the financial markets, was performing an important public duty and must therefore be subject to judicial review like any other public body. The former Master of the Rolls argued in particular with the willingness of the Secretary of State for Trade and Industry to limit legislation in the field of takeovers and mergers and to use the Panel as the centrepiece of his regulation of that market.¹²⁷ Thus, the innovative *Datafin* decision made for the first time clear that the essential distinction

125 Ibid, at p. 842; *Aldous/Alder*, Applications for Judicial Review, p. 7-30.

126 R. v. Electricity Commissioners, ex parte London Electricity Joint Committee (1920) Ltd., [1924] 1 K.B. 171, 205; *Forsyth*, The Scope of Judicial Review, [1987] P.L. 356, 361.

127 R. v. Panel on Takeovers and Mergers, ex parte Datafin Plc. [1987] QB 815, 838.

between a private and a public law body lies not exclusively in its source of power, but also in the nature of the power exercised. If the body in question is performing a public duty, then that may be sufficient to bring the body within reach of judicial review.¹²⁸

(b) The Practical Issue

Because of the Panel's unique character and the special nature of the financial markets on the one hand and the discretionary nature of judicial review on the other hand, it had to be decided in which way the judicial discretion would be exercised to interfere with the Panel's decisions. Broadly speaking, a much wider and far less interventionist approach has been applied than in the case of "normal" statutory public bodies. In *Datafin* the Court of Appeal held that during the course of a bid intervention by the courts would be rare. The Court of Appeal stated that the relationship between the courts and the Panel would be "*historic rather than contemporaneous*".¹²⁹ The court would allow the "*contemporary decisions to take their course, considering the complaint and intervening, if at all, later in retrospect by declaratory orders which would enable the Panel not to repeat any error and would relieve individuals of the disciplinary consequences of any erroneous finding of breach of the rules*".¹³⁰ Moreover, an application for judicial review would *not* lead to a suspension of the Panel's decision as is often the case with statutory public bodies. It is to be treated as valid and binding until and unless it is set aside. The Court of Appeal also stressed that the Panel should be given "considerable latitude" in interpreting the Code.¹³¹ Lord Donaldson M.R. concluded that the

128 Ibid, at p. 847.

129 Ibid, at p. 842.

130 Ibid, at p. 838.

131 Ibid, at p. 841.

only event in which he could imagine the use of the remedies of certiorari and mandamus would be a breach of the rules of natural justice. The Court of Appeal justified this restrictive approach mainly with the "*special nature of the Panel, its functions, the market in which it is operating, the time scales which are inherent in that market and the need to safeguard the position of third parties*". A further justification was to prevent an appeal to the court from being used as a defensive ploy to thwart or impede a bid.¹³²

As a view across the Atlantic demonstrates,¹³³ the excessive use of tactical litigation has in the long term harmful consequences for most parties involved.¹³⁴ It has therefore been wise to limit the susceptibility of the Panel's decisions to judicial review. However, one is forced to ask whether the now established balance between the smooth functioning of the takeover process on the one hand and the rights of a possibly gravely aggrieved party by an erroneous Panel decision on the other hand is not severely biased towards the interests of the Panel. Since the decisions of the Panel are practically unchallengeable during the course of a bid, a wrongly aggrieved party has to have recourse to a mere declaratory order after the takeover process has ended. But a declaratory order, which after all is mainly designed to prevent the Panel from future errors, is surely of relatively little use to any aggrieved party after the takeover has ended. The fact that an appeal against the Panel Executive can be made to the full Panel and the Panel's Appeal Committee may be some form of compensation for the *de facto* non-availability of judicial review during a bid. However, as the examination of this issue,¹³⁵ in particular Table 9 at page 41, has demonstrated, an appeal to the full Panel or the Appeal Committee has very little chance of success indeed. Moreover, neither the full Panel nor the

132 Ibid, at p. 840.

133 *Solomon/Schwartz/Baumann*, Corporations, p. 1031, 1143.

134 *Lord Alexander of Weedon*, Takeovers: The Regulatory Scene, [1990] J.B.L. 203, 214.

135 See Chapter 3.1.2.(2) at page 41.

Appeal Committee can be likened to an independent court. Both Panel procedures are ultimately internal procedures with the Panel as judge in its own cause. It is rather indicative that *Lord Alexander of Weedon* Q.C. argued in his former capacity as Counsel for the Panel in the *Datafin* case fiercely against the allegedly disastrous consequences of the Panel being susceptible to judicial review, whereas he was having nothing but praise for that very decision - which after all had turned against him - in his later function as chairman of the Panel.¹³⁶ It would very much seem that although he formally lost the case he eventually won it in substance as the *Datafin* decision while formally allowing judicial review restricted it in practical terms to an almost useless right. In this context, it is needless to say that no application for judicial review against the Panel has ever been successful,¹³⁷ and under the circumstances described above it is difficult to believe that an intervention by a court by way of orders of certiorari or mandamus against the Panel will ever take place during the course of a bid. However excellent the Panel's work generally may be, in consideration of the enormous power it enjoys and the negligible role played in practice by the Panel's Appeal Committee,¹³⁸ the control exercised by the courts seems rather inadequate.

136 *Lord Alexander of Weedon*, *Judicial Review and City Regulators*, (1989) 52 MLR 640, 644, 648; and *Takeovers: The Regulatory Scene*, [1990] J.B.L. 203, 214.

137 See *R. v. Panel on Takeovers and Mergers, ex parte Datafin Plc.* [1987] QB 815; *R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc.* [1989] 1 All ER 509; *R. v. Panel on Takeovers and Mergers, ex parte Fayed and others*, [1992] BCLC 938.

138 See Table 9 at page 41.

3.1.3. The Rules Governing Substantial Acquisitions

The Rules Governing Substantial Acquisitions of Shares (SARs) are the second major set of rules which is administered by the Panel. They first came into force in 1981, then published by the Council for the Securities Industry (CSI).¹³⁹ As the CSI wound itself up in 1985 in order to make room for the new regulatory system which was due to be established by the Financial Services Act 1986, the Panel became responsible for the SARs. The SARs contain five Rules each followed by a number of Notes. They are administered and enforced¹⁴⁰ in the same way as the City Code and publicised together with it.¹⁴¹

The SARs are designed to restrict so called "dawn raids", i.e. the rapid acquisition of a substantial strategic stake in a target company listed on the Stock Exchange within a matter of minutes.¹⁴² Unrestricted dawn raids are considered undesirable. Because of the speed in which they are carried out, only institutional shareholders get the chance to sell at the increased dawn raid-price whereas small investors are left out in the cold. In case of a dawn raid, the City Code does not apply unless the acquisition results in the

139 As to history see *Palmer's Company Law*, para 12.345.

140 An interesting example for a clear breach of Rule 1 of the SARs is the case of Bowater. Bowater bought on January 11, 1989 0.6 per cent in Norton Opax shares in the market and a further 23.6 per cent later on the same day from Bishopsgate Investment Trust. In fear of a full takeover by Bowater, Norton Opax complained to the Panel and argued that Bowater should be required to reduce its shareholding to below 15 per cent to remedy the breach of Rule 1. The Panel, however, ruled that under the special circumstances of the case it was sufficient for Bowater to dispose of the 0.6 of Norton Opax shares bought in breach of the SARs. See Panel Statement on February 2, 1989, [1989] J.B.L. 148.

A further example of a breach of Rule 1 and 3 of the SARs is the case of Timpson plc with Henry Cooke as their advisers; see Panel Statement on Timpson plc/Automagic Holdings plc, May 8, 1990, [1991] J.B.L. 65.

141 See 3.1.2. (3).

142 Begg, *Corporate Acquisitions*, para 9.88; *Palmer's Company Law*, para 12.346; *Weinberg/Blank*, *Takeovers*, para 3-901 et seq.

acquirer holding 30 per cent or more of the voting rights in the target company, in which case Rule 9 of the City Code triggers a mandatory bid to all shareholders. Following a particularly aggressive dawn raid for *Consolidated Goldfields Ltd* shares¹⁴³ in February 1980, the SARs were set up to secure fair and equal treatment of all shareholders in the areas where the Code is not applicable.¹⁴⁴ The effect of the SARs is basically twofold:

First, they slow down the speed with which a person is able to increase his holding of shares to an aggregate of between 15 and 30 per cent.¹⁴⁵ Under Rule 1 of the SARs a person may not acquire within any period of seven days 10 per cent or more of the voting rights of a company if that takes his stake to an aggregate of between 15 and 30 per cent. Below 15 per cent dawn raids remain unrestricted and from 30 per cent on the City Code takes over as stated above. According to Rule 2 of the SARs the restrictions in Rule 1 do not apply where the acquisition is made from a single shareholder or where it is pursuant to a tender offer.¹⁴⁶ Moreover, the SARs are inapplicable immediately before a person announces a firm intention to make an offer and they remain inapplicable until the offer has become unconditional as to acceptances, or lapses or is withdrawn.¹⁴⁷

The second effect of the SARs is to promote accelerated disclosure of acquisitions in order to prevent the building of

143 On February 11 Gold Field shares stood at 525p. When trading started the following morning the price was quoted 615/617p and by 10.00 am brokers acting for Angelo/De Beers had purchased 16.5 million shares at 616p. Purchases ceased and the price fell back to 510p. See *Morse*, Panel Report for the year ended March 31, 1980, [1980] J.B.L. 359.

144 *Weinberg/Blank*, Takeovers, para 3-902.

145 *Weinberg/Blank*, Takeovers, para 3-903.

146 As to tender offers see Rule 4 of the SARs. A tender offer is a firm offer to buy a specified number of shares for cash only. Other than a partial bid under the City Code, a tender offer is published by paid advertisement in two national newspapers and no offer documents are sent to the shareholders. See *Palmer's Company Law*, para 12.349; *Weinberg/Blank*, Takeovers, para 3-906 et seq.

147 See SARs, Introduction, para 2.

substantial stakes by stealth.¹⁴⁸ Under Rule 3 of the SARs the acquirer must notify his acquisition and holding in aggregate to the target company and the Stock Exchange, which in turn will notify the Panel, by 12 noon on the following business day if his acquisition results in him holding 15 per cent or more of the voting rights or if his holding increases by a whole percentage point over 15 per cent. However, there is a considerable overlap with the disclosure requirements of the Companies Act 1985 under which disclosure is required when a person holds 3 per cent of the voting shares in a company together with any significant change in his holding above the 3 per cent threshold.¹⁴⁹ The justification for the disclosure requirements in the SARs lies therefore mainly in the fact the Companies Act 1985 allows 2 days for notification whereas notification under the SARs must be made before 12 noon on the following business day.¹⁵⁰

3.1.4. The Rules of the Stock Exchange

Another important source of rules governing certain aspects of takeovers are the regulations of the Stock Exchange. The Stock Exchange is the "competent authority"¹⁵¹ responsible for the conduct of the U.K. securities market. The most important securities market segment is the listed market which is a market in shares admitted to the "Official List" of the Stock Exchange.¹⁵² The relevant rule book

148 *Weinberg/Blank*, Takeovers, para 3-909.

149 Section 199 (2) CA 1985.

150 Section 202 (1) CA 1985; see also *Weinberg/Blank*, Takeovers, para 3-905.

151 Section 142 (6) FSA 1986.

152 The second market segment, the Unlisted Securities Market (USM), is designed to allow smaller companies to raise capital without the formalities and expenses of a full listing. The USM is regulated by the Stock Exchange's "Green Book", the latest edition of which entered into force on 30 June 1994. However, since the USM is going to be phased out in 1996 and replaced by the Alternative Investment Market (AIM), which opened in June 1995, the following paras will only deal with the

governing the listed market is the so called "Yellow Book" of the Stock Exchange.¹⁵³

Historically, the nature of the Yellow Book had been entirely self-regulatory. Yet, this has changed under the influence of European legislation.¹⁵⁴ In order to implement three EC-Directives, the government pronounced in May 1984 via Statutory Instrument the "Stock Exchange Regulations"¹⁵⁵ which in turn were incorporated in a revised edition of the Yellow Book by the Stock Exchange in November 1984. Hence, from that time on, the Yellow Book-requirements are partly based on statutory provisions and partly reflect the Stock Exchange's own rules.¹⁵⁶ The Stock Exchange Regulations 1984 were replaced by Part IV of the Financial Services Act 1986 and accordingly a new edition of the Yellow Book was issued by the Stock Exchange in 1987.

In December 1993 an entirely remodelled version of the Yellow Book¹⁵⁷ came into force¹⁵⁸ which is mainly designed to make the Yellow Book more user-friendly and to incorporate practices and interpretations which had become established over the years.¹⁵⁹ It is divided into 25 chapters preceded by an introduction and supplemented by 11 schedules. Broadly speaking, the Yellow Book

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- Yellow Book. References to the Green Book are made in footnotes. As to the USM and AIM see for further references Chapter 3, footnote 4.
- 153 Until the new 1993 edition the Yellow Book was formally entitled "Admission of Securities to Listing Rules".
- 154 Broadly speaking, the following Directives are designed to harmonise the conditions on which companies may be floated and regulated on Stock Exchanges within the EU. For details see *Palmer's Company Law*, para 5.403.
Admissions Directive, No. 79/279/EEC;
Listing Particulars Directive, No. 80/390/EEC;
Interim Reports Directive, No. 82/121/EEC.
- 155 S.I. 1984 No. 716.
- 156 *Begg, Corporate Acquisitions*, para 9.15; *Weinberg/Blank, Takeovers*, para 3-524.
- 157 Now formally called "The Listing Rules of the Stock Exchange".
- 158 Updated by Amendment No. 1 which took effect on March 10, 1994. Reproduced in *Palmer's Company Law*, 25th edition, Vol. 2, Part C.
- 159 *Begg, Corporate Acquisitions*, para 9.15.

aims to secure the confidence of investors in the conduct of the market.¹⁶⁰

In a takeover, the Yellow Book may become relevant in two ways: First, where the issue of new shares for which listing is sought is used by the offeror as consideration for the acquisition. Secondly, the Yellow Book imposes certain "continuing obligations" on the companies which have obtained a full listing on the Stock Exchange. These continuing obligations also contain a number of provisions relevant in a takeover.

(1) Listing Particulars

Based on Part IV of the Financial Services Act 1986 large parts of the Yellow Book are concerned with the requirements to be observed when new shares are issued either by new applicants or by companies whose shares are already listed.¹⁶¹ Frequently, a takeover offer contains as consideration for the acquisition a share-option which involves the issue of new shares for which listing is sought.¹⁶² Consequently, listing particulars are required¹⁶³ unless the new shares would increase the shares of a class already listed by less than 10 per cent.¹⁶⁴

160 See Yellow Book, Introduction; *Weinberg/Blank*, Takeovers, para 3-524; *Palmer's Company Law*, para 5.408.

161 Offers to the public where listing is not sought are governed by *The Public Offers of Securities Regulations 1995* (SI 1995/1537).

162 See *Weinberg/Blank*, Takeovers, para 2-051 et seq. Pre-emption rights do not apply to an issue of equity shares for a non-cash consideration, section 89 (4) CA 1985.

163 Concerning listing particulars in a takeover see expressly paras 10.46 and 10.47 of the Yellow Book. As to listing particulars in general see chapter 5 and 6 of the Yellow Book.

164 Para 5.27 (e) of the Yellow Book.

The precise and detailed information required by the listing particulars is set out in chapter 6 of the Yellow Book¹⁶⁵ and contains basically information about the persons responsible for the listing particulars¹⁶⁶, the shares for which listing is sought¹⁶⁷, the issuer and its capital¹⁶⁸, the group's activities¹⁶⁹, the issuer's assets and liabilities, its financial position and profits and losses¹⁷⁰, the management¹⁷¹, and the recent development and prospects of the group.¹⁷²

(2) Continuing Obligations

All listed companies are subject to "continuing obligations" imposed by chapter 9 and the following seven chapters of the Yellow Book. Of great importance to a listed bidder are chapters 10 and 11 entitled "Transactions" and "Transactions with Related Parties" respectively.¹⁷³ Transactions, i.e. acquisitions and disposals, carried out by listed companies are classified into 6 different categories: Super Class 1¹⁷⁴, Class 1¹⁷⁵, Class 2¹⁷⁶, Class 3¹⁷⁷, Reverse Takeovers¹⁷⁸, and Transactions with Related Persons¹⁷⁹. Apart from transactions with related persons, the categories are, broadly

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- 165 The requirements concerning the prospectus imposed by the Green Book are compared to those of the Yellow Book considerably less demanding. See *Begg*, Corporate Acquisitions, para 9.56.
 - 166 Chapter 6A of the Yellow Book.
 - 167 Chapter 6B of the Yellow Book.
 - 168 Chapter 6C of the Yellow Book.
 - 169 Chapter 6D of the Yellow Book.
 - 170 Chapter 6E of the Yellow Book.
 - 171 Chapter 6F of the Yellow Book.
 - 172 Chapter 6G of the Yellow Book.
 - 173 *Begg*, Corporate Acquisitions, para 9.19; *Weinberg/Blank*, Takeovers, para 3-527.
 - 174 Para 10.37 of the Yellow Book.
 - 175 Para 10.35 of the Yellow Book.
 - 176 Para 10.31 of the Yellow Book.
 - 177 Para 10.29 of the Yellow Book.
 - 178 Para 10.39 of the Yellow Book.
 - 179 Para 11.1 et seq. of the Yellow Book.

speaking, defined in terms of size of the transaction relative to the size of the company. According to the category to which a transaction belongs, different requirements are set out concerning circulars and shareholder approval.¹⁸⁰ The larger the transaction in relation to the company, the more demanding are the obligations imposed by the Yellow Book.¹⁸¹

Yet, an accurate description of the elaborate and complex method by which the size of a transaction is assessed and the details of the different requirements would be beyond the scope of this work.

3.1.5. Legal Provisions in the Companies Act 1985

Although Part XIII A of the Companies Act 1985 is somewhat promisingly entitled "Takeover offers", the Act regulates only few confined, but nevertheless noteworthy aspects of a bid.

(1) Compensation for Loss of Office

Compensation for loss of office¹⁸² may under section 314 of the Companies Act 1985 be paid to a director who has lost his office in connection with a takeover only if the particulars of the payment are

180 For details see the very clear description in chapters 10 and 11 of the Yellow Book. Also *Begg*, Corporate Acquisitions, para 9.19 et seq. and *Weinberg/Blank*, Takeovers, para 3-527 et seq.

181 The Green Book works in principle in a similar way, but lessens the requirements considerably. See *Begg*, Corporate Acquisitions, para 9.56.

182 As stated in section 316 (3) CA 1985 compensation for loss of office does not include the payment of damages for breach of his employment contract or as consideration for his retirement from office. Generally, any payment to which the company is legally obliged can not be considered as compensation for loss of office.

disclosed to the shareholders and approved by them in general meeting. Any sum received by a director in contravention of that provision is deemed to have been received by him in trust for the former shareholders who have sold their shares as a result of the offer: section 315 of the Companies Act 1985.¹⁸³

It is clear from the wording of section 314 that it does not apply if the receiving director of the target company remains in office. This seems somewhat unfortunate since in such a way undisclosed payments could theoretically be used by the offeror company to gain undue influence upon the target board directors, e.g. to induce them to recommend favourably the offer to the shareholders.¹⁸⁴ However, any such arrangement would clearly infringe the City Code on Takeovers and Mergers.¹⁸⁵ Furthermore, as a secret profit would have been made by this director, the question of a breach of the director's fiduciary duties towards the target company would arise.¹⁸⁶ Contrary to section 315 of the Companies Act 1985, and this constitutes an important difference, the beneficiary of any action brought against the defective director would be the company, and not the former shareholders.

(2) Compulsory Transactions

Since the Companies Act 1929¹⁸⁷ the right of an offeror company to buy out dissenting minority shareholders after a

183 *Palmer's Company Law*, para 12-201.

184 Concerning the duties which the target board directors owe to the shareholders in relation to advice in a takeover battle see *Gething v. Kilner* [1972] 1 All ER 1166.

185 General Principal 5 which requires that any information given to the shareholders by either the offeror or the offeree board must "be prepared with the highest standards of care and accuracy."

186 As to a director's duty not to make a secret profit see *Regal (Hastings) Ltd. v. Gulliver* [1967] 2 A.C. 134.

187 Section 155 of the CA 1929. As to history see *Weinberg/Blank*, Takeovers, para 3-872.

successful takeover compulsorily when 90 per cent or more of the shareholders to which the offer has been made have accepted the offer has been a feature of English company law. The offeror's right to buy out dissenting shareholders compulsorily was later complemented by the minority shareholders' right to be bought out once the acquirer has reached the 90 per cent threshold. The relevant provisions are now set out in detail in Part XIII A of the Companies Act 1985: sections 428 to 430F.¹⁸⁸

The terms on which the offeror is entitled or compelled, as the case may be, to buy the minority shares are as a general rule exactly the terms of the previous offer.¹⁸⁹ However, both parties may apply to the court which has discretion to decide upon the matter. Where the offeror is trying to buy out a minority shareholder compulsorily, the court may, on application of the respective shareholder, order that the offeror is not entitled to buy the shares compulsorily or specify the terms of the compulsory acquisition different from that of the offer.¹⁹⁰ Where a minority shareholder wishes to be bought out by the offeror the court may, on application of either party, order that the terms of the forced acquisition shall be such as the court thinks fit.¹⁹¹ However, bearing in mind that the overwhelming majority of shareholders have accepted the offer which can usually be seen as a clear indication of the fairness of the offer, the courts will generally be reluctant to interfere.¹⁹²

In terms of policy, the discussed provisions, which are mainly designed to tidy up the aftermath of a successful bid, seem

188 A procedure which bears some resemblance to these provisions is contained in sec. 320 of the German Stock Corporations Act (AktG). The majority required for such a "*Eingliederung*" is 95 per cent. As a result of the *Eingliederung* the parent company may give directions to the management board of the subsidiary, sec. 323, 309 AktG.

189 Sections 429 (2) and 430B (2) CA 1985.

190 Section 430C (1) CA 1985.

191 Section 430C (3) CA 1985.

192 *Re Carlton Holdings* [1971] 2 All ER 1082. An illustrative example for the Court of Appeal preventing an compulsory acquisition because of improper use of this right is *Re Bugle Press Ltd.* [1960] 3 All ER 791. See also *Palmer's Company Law*, para 12.213.

ambivalent. On the one hand, what in effect takes place is an expropriation of private property for the sake of the business interests of another private person or company. On the other hand, every purchase of shares in the U.K. is from the outset on made under the conditions imposed by law amongst which are the respective provisions of the Companies Act 1985. From the target shareholder's point of view, the knowledge of the right to be bought out on the offer conditions prevents him from being forced to accept the offer for fear of getting a less favourable treatment than an approving shareholder¹⁹³ or being locked in.¹⁹⁴ Moreover, the procedure of compulsory acquisition provides for the offeror to get hold of the shares of holders who are untraceable which is an important practical aspect.¹⁹⁵

3.2. Structural Barriers

The high incidence of public takeover bids in the U.K. suggests that not many structural barriers exist. Numerous most spectacular bids could be witnessed during the time of writing this thesis of which only a few can be mentioned here: In September 1994 *British Aerospace* launched an agreed £480 million bid for the submarine maker *VSEL* which was rivalled in October 1994 by a competing £532 million offer from *GEC*.¹⁹⁶ *Trafalgar House* made a £1.2 billion offer for *Northern Electric*, a recently privatised utility, in December 1994 which was immediately fiercely rejected by the offeree board.¹⁹⁷ In January 1995, *Glaxo Holdings*, the world's largest drugs

193 Re Carlton Holdings [1971] 2 All ER 1082.

194 *Weinberg/Blank*, Takeovers, para 3-873, footnote 7.

195 Section 430 (11) CA 1985 under which the consideration for these shares is ultimately paid into court. See also *Palmer's Company Law*, para 12.212: If the offeror does not reach the 90 per cent threshold because of untraceable shareholders, he may apply to the court.

196 *Financial Times*, November 19, 1994.

197 *Times*, December 20, 1994.

company, launched a hostile £8.9 billion bid for its rival *Wellcome*.¹⁹⁸ A number of bids were made in the electricity sector. The *Southern Company*, a huge American utility company, launched a £1 billion hostile offer for *South Western Electricity*, another of the recently privatised utilities,¹⁹⁹ in July 1995 prompting an outcry in parts of the British press.²⁰⁰ *Hanson* offered £2.5 billion for *Eastern Group*,²⁰¹ and *Scottish Power* launched a £1 billion hostile bid for *Manweb*.²⁰² Neither of these rather controversial electricity bids were referred to the Monopolies and Mergers Commission for an in-depth investigation.²⁰³ In April 1996, however, *Ian Lang*, the trade and industry secretary blocked, however, the bid by *National Power* for *Southern Electricity* and *Powergen's* offer for *Midlands Electricity* (against the advice of the Monopolies and Mergers Commission and his own officials).²⁰⁴ In January 1996 *Granada* finally triumphed in a bitter £3.9 billion fight for *Forte*.²⁰⁵ To end this list which could be substantially extended, in April 1996 *Rentokil* claimed victory in the hostile £2.2 billion takeover of *BET*.²⁰⁶

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- 198 *Times*, January 1, 1995. Taking into account the share options the offer amounts to £9.4 billion. See *Times*, January 27, 1995.
- 199 *Times*, July 11 and July 15, 1995.
- 200 See, for example, the *Daily Mirror*, 26 August 1995, at p. 6: "The takeover of South Western Electricity is outrageous. ... Why do people of the very English counties of Devon, Cornwall and Somerset need to have their electricity provided by a US firm? They don't, of course. But this is only the first step in a foreign takeover of the nation's vital public utilities. The French are already after our water. Other foreign firms will soon pitch in to get their hands on huge profits of the electricity and water monopolies. When these industries were privatised, the Tories claimed it would put power into the hands of customers. Instead it is leading to control being handed to faceless bosses thousands of miles away. ... The Monopolies Commission could stop this takeover and it should. That would demonstrate to foreign predators that there are not easy pickings in our privatised utilities."
- 201 *Times*, 31 July 1995.
- 202 *Times*, 25 July 1995; 1 September 1995.
- 203 *Times*, 1 September 1995: "Electricity bids win surprise go-ahead".
- 204 *Financial Times*, 16 May 1996: "Minister's decisions on bids baffle power industry."
- 205 *Financial Times*, 19 January 1996, 24 January 1996.
- 206 *Financial Times*, 27/28 April 1996. Mr Luther John Clark, the sacked executive of BET, is currently claiming £4 million in compensation for unfair dismissal in court, see *Financial Times*, 14 October 1996.

Nevertheless, in terms of structural takeover barriers the requirement of a mandatory offer and the provisions designed to prevent dawn raids seem worth mentioning.

3.2.1. Requirement of a Mandatory Bid

To identify Rule 9 of the City Code, which requires an offer to be made to all shareholders of the target company once the 30 per cent threshold is passed,²⁰⁷ as a structural barrier to takeovers may perhaps be surprising from the British point of view. However, Rule 9 imposes a restriction on the freedom to acquire shares and it can not be denied that its economic effect is to make the acquisition of control as defined by the City Code²⁰⁸ more expensive. Rule 9 might be favourable for large companies who can afford making a 100 per cent offer; it is a disadvantage for smaller less potent companies. Less expensive partial offers intended to result in the offeror holding less than 100 per cent are not permitted in Britain except with the consent of the Panel; and even if the Panel's permission can be obtained further requirements are to be met.²⁰⁹

In Germany, the mandatory offer rule is despite recent changes in connection the new voluntary German Takeover Code 1995²¹⁰ widely seen as an inappropriate restriction on the freedom to acquire shares.²¹¹ Although the German Stock Corporations Act 1965

207 See Chapter 3.1.1. (2)(a) at pp. 32. The *Trade and Industry Committee Report on Takeovers and Mergers*, 1991, para 150 has even recommended to Lower the mandatory bid threshold to 20 per cent.

208 The City Code (Definitions) defines the term control as follows: "*Control means a holding, or aggregate holdings, of shares carrying 30 per cent or more of the voting rights (as defined below) of a company irrespective of whether the holding or holdings gives de facto control.*"

209 Rule 36.1 City Code. Also Gower's *Principles of Modern Company Law*, pp. 723.

210 See in more detail Chapter 4.1.1.(4) at pp. 116.

211 Grunewald, *Der geänderte Vorschlag einer 13. EG-Richtlinie*, WM 1991, 1361, 1362; Hommelhoff/Kleindiek, *Takeover Richtlinie*, AG 1990, 106, 109; Mertens, *Förderung von, Schutz vor, Zwang zu*

requires the management of a company to treat its *own* shareholders equally,²¹² there is no legally binding rule defining equality in the context of a takeover or providing that a bidder must treat the target shareholders equally (however defined).²¹³ Consequently, the German delegation in Brussels has always strongly rejected the inclusion of a mandatory bid rule in a future European Takeover Directive.²¹⁴ Hence, it is safe to say that when it comes to acquiring shares the view that all shareholders should participate in a premium paid for control is not generally shared in Germany.²¹⁵ It is standard practice for companies to seek effective control of another company by simply acquiring a simple majority of shares or a blocking majority without having to make an offer and pay a premium for corporate control to all shareholders. It is obvious that the present situation in Germany is to the detriment of small investors who never ever have the chance to participate in premiums. This in turn damages the equity market as a whole²¹⁶ in that small investors are averse to

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- Übernahmeangeboten, AG 1990, 252, 256. For further details see Chapter 5.1.1.(2) at p. 177.
- 212 Sec. 53a AktG. This provision is based on Art. 42 of Directive 77/91/EEC of 13 December 1976, [1977] O.J. L 26/1, but the principle of equal treatment in the company-shareholder relationship had long been generally acknowledged as a fundamental company law principle before the introduction of sec. 53a AktG.
- 213 For a thorough analysis of this issue see *Reul*, Die Pflicht zur Gleichbehandlung der Aktionäre bei privaten Kontrolltransaktionen, pp. 250.
- 214 See Chapter 5.1.1.(2) at pp 177 and concerning the 1996 proposal for a European Takeover Directive Chapter 5.1.2.(3)(b) at pp. 191.
- 215 Against a participation in the premiums are, for example, *Grunewald*, Der geänderte Vorschlag einer 13. EG-Richtlinie betreffend Übernahmeangebote, WM 1991, 1361, 1363; *Hommelhoff/Kleindiek*, Takeover-Richtlinie und europäisches Konzernrecht, 1990, 106, 108; *Lutter*, Die Treuepflicht des Aktionärs, ZHR 153 (1989), 446, 462; *Lüttmann*, Kontrollwechsel in Kapitalgesellschaften, 1992, S. 180; *Mertens*, Förderung von, Schutz vor, Zwang zu Übernahmeangeboten, AG 1990, 252, 256; *Sandberger*, Teilübernahmeangebote und Zwangsübernahmeangebot im Europäischen Takeover Recht, DZWIR 1993, 319, 323; critical also *Baums*, Übernahmeregeln in der Europäischen Gemeinschaft, ZIP 1989, 1377, 1379. In favour of a participation are, however, *Berger*, Unternehmensübernahmen in Europa, ZIP 1991, 1644, 1652; *Otto*, Die Verteilung der Kontrollprämie bei Übernahme von Aktiengesellschaften, AG 1994, 167; for a very thorough analysis of the issue see *Reul*, Die Pflicht zur Gleichbehandlung der Aktionäre bei privaten Kontrolltransaktionen, 1991, 300. See also Chapter 5.1.1.(2) at p. 177.
- 216 *Financial Times*, 18 December 1992: German takeover rules criticised.

investing in equities, a fact that is clearly reflected in the stock market comparison provided in Chapter 2.²¹⁷

Considering the somewhat unsatisfactory stock-market situation and standard of equality in Germany,²¹⁸ it seems that there are at least very good reasons justifying a mandatory offer requirement. From a British standpoint, it might well be argued that the standard of shareholder equality is minor in Germany and it is interesting to note that the present German situation is quite similar to the British state of affairs before the introduction of the City Code in 1968.²¹⁹ But whatever one's opinion about mandatory offers is, it must be acknowledged that this "barrier" does not render a takeover impossible, it just makes it more expensive and is therefore quite different from barriers existing in other European countries, most notably the Netherlands and Germany.²²⁰

3.2.2. Restrictions on Stake-Building

A somewhat minor "barrier" which also has no equivalent in German law are the *Rules Governing Substantial Acquisition of Shares* (SARs) which have been discussed earlier²²¹ and whose effect mainly is to slow down the speed with which an investor is able to increase his holding to an aggregate of between 15 and 30 per cent to prevent dawn raids. Again, this "barrier" does not render a bid impossible, but simply restricts the bidders freedom to prevent abuses. The previously explained purpose of these rules, namely to

217 See in particular Table 2 at p. 19.

218 As to the City Code see Chapter 3.1.1.(2)(a) at pp. 32. Regarding the German Takeover Code see Chapter 4.1.1.(3)(a) at pp. 112.

219 As to the pre-Code era see *Weinberg/Blank*, Takeovers, para 3-909.

220 Regarding German barriers see Chapter 4.2. at pp. 132. As to the mandatory bid requirement, shareholder equality and the protection of minorities under the proposed Takeover Directive see Chapter 5.1.2.(3) at pp 188.

221 See Chapter 3.1.3. at pp. 56.

give small investors a chance to participate in premiums paid, justifies the restriction.

3.3. Protective Measures in Advance of a Bid

Before analysing the defensive - or rather protective - measures available to directors in advance of a bid it seems appropriate to outline briefly the duties of directors involved in creating such obstacles and "poison pills".²²² The City Code's non-legal provisions banning any defensive action by the target board do not apply in the period before a bona fide offer has been communicated or is imminent.²²³ If a company is not in any actual bid situation, the Code is not applicable and the common law duties of directors are to be observed together with few statutory provisions.²²⁴ As a company is regarded as the property of its shareholders, the directors are under a fiduciary duty to act "*bona fide in what they consider - not what a court may consider - is in the interests of the company, and not for any collateral purpose*".²²⁵ In *Hogg v. Cramphorn* it was further established that the directors had not only to act in good faith, which imposes a subjective test, but also for a proper purpose, i.e. a purpose for which the power exercised was - objectively - conferred on them.²²⁶ However, since many of the protective measures and transactions discussed in this chapter may well be entered into for proper purposes in the ordinary course of business it will in practice

222 For a thorough analysis of these issues see Parkinson, *Corporate Power and Responsibility*, p. 140 et seq.

223 General Principal 7 and Rule 21 of the Code. See Chapter 3.1.1.(2)(d) at p. 35.

224 See, for example, section 309 CA 1985 (Directors to have regard to interests of employees).

225 Per Lord Greene M.R. in *Re Smith & Fawcett Ltd.* [1942] Ch. 304 at p. 306.

226 *Hogg v. Cramphorn* [1967] Ch. 254.

often be extremely difficult to prove that the directors did not act bona fide for a proper purpose, especially if they act well in advance of any actual bid.²²⁷ The topics discussed below only represent the issues which the author considered most relevant and are not all-embracing.

3.3.1. Unequal Voting Rights

Compared to the regulation in the German Stock Corporation Act, English company law is more liberal concerning weighted voting rights as the following analysis shows.²²⁸ A voting structure different from "one share - one vote" leads to some shareholders having an influence on the company which is disproportionate to their investment. Special voting powers attached to a certain class of shares held by a special group of shareholders, e.g. the directors of the company, a certain family or the government in form of a "*golden share*" in a privatised company,²²⁹ may well be used to make a company bid-proof.

In *Bushell v. Faith*,²³⁰ the articles stipulated that on a resolution to remove a director, that director should carry three votes per share, which in that case rendered it impossible for the remaining shareholders to remove *Mr Faith* as a director. At first instance, an

227 *Prentice*, Regulation of Takeover bids, p. 157; *Weinberg/Blank*, Takeovers, para 3-786.

228 See on the one hand Reg. 2 Table A of the CA 1985: "*Subject to the provisions of the Act and without prejudice to any rights attached to any existing shares, any share may be issued with such rights or restrictions as the company may by ordinary resolution determine.*" and section 12 of the German Stock Corporation Act on the other hand in APPENDIX 2. As to the relatively popular voting restrictions in Germany see Chapter 4.3.1. at p. 157.

229 For a recent example in which the U.K. government threatened to use its "golden shares" in two electricity companies, *National Power* and *PowerGen*, in connection with a bid by a U.S. company, *Southern*, see *Financial Times*, 3 May 1996: *U.K. to block bids for generators with 'golden share'*. See also *Dine*, EC Company Law, para 15.9.

230 [1969] 1 All ER 1003.

injunction was granted on the basis that such a provision infringed the right to remove a director by ordinary resolution.²³¹ However, the Court of Appeal and the House of Lords took a different view²³² and the provision in the articles was upheld which made *Mr Faith's* position as director unimpeachable.

Another case illustrating some aspects of the problem is *Re Savoy Hotel Ltd.*²³³ After the battle for control of that company had been resolved a class of equity capital was created which represented less than 3 per cent of the entire capital, but had the power to outvote all other shareholders representing 97 per cent of the capital.

In Germany, after rather dreadful experiences with weighted voting rights in the 1920s where it occurred that special shares outvoted ordinary shares more than ten thousand times, section 12 (2) of the Stock Corporation Act 1965 was introduced which stipulates that multiple voting rights attached to a share are not permitted except with consent of the Ministry of Economic Affairs in the Bundesland where the company has its corporate seat.²³⁴ The ministerial permission may only be granted if weighted voting rights are necessary to safeguard the overall economic interest of the public, especially where sensitive industrial sectors such as the defence or power industry are concerned.²³⁵ Very few ministerial permissions have been granted so far,²³⁶ and many academics are

231 See now section 303 Companies Act 1985; then section 184 of the Companies Act 1948.

232 As to criticism of this decision see *Palmer's Company Law*, para 8.033.

233 [1981] Ch. 351.

234 Moreover, a majority of 75 per cent is required to introduce weighted voting rights, section 179 (2) AktG. As far as the popular restriction of voting rights in Germany is concerned see 4.3.1. at p. 157.

235 As to further references see *Zöllner/Noack*, One share - one vote? AG 1991, 117, 130. In Britain the Industry Act 1975 empowers the government to block changes of control in important manufacturing undertakings if non-U.K. residents are involved.

236 19 permissions until 1989.

rightly of the opinion that weighted voting rights should be abolished entirely in Germany.²³⁷

Although English company law permits multiple voting rights which might constitute a serious barrier to takeovers of non-listed companies, only very few listed companies do have weighted - or in fact otherwise unequal - voting rights.²³⁸ The Stock Exchange discourages such practices, though they are not formally prohibited by the Yellow Book and there exists no strict "*one share - one vote*" rule.²³⁹ Moreover, institutional investors exercise additional pressure against any form of weighted or restricted voting rights since this would reduce the institutions' influence.²⁴⁰ As far as listed companies are concerned, weighted voting rights do therefore not constitute a serious practical barrier to takeovers in Britain.

On the European level, Article 33 of the proposed Fifth Directive would - if passed - prohibit weighted voting rights in public limited companies.²⁴¹

237 See references in *Zöllner/Noack*, One share - one vote? AG 1991, 117, 129 who themselves want to maintain the present regulation to protect German industry against harmful investors.

238 The only exception are not voting preference shares which, however, do not constitute a particular barrier to takeovers. To the disadvantages of preference shares see *Weinberg/Blank*, Takeovers, para 3-800 et seq.

239 *Prentice*, Regulation of Takeover bids, p. 152; *Boyle*, Barriers to Contested Takeovers in the EC, *Company Lawyer*, Vol. 12, No. 9, p. 163, 164 (1991).

240 *Weinberg/Blank*, Takeovers, para 3-805.

241 As to the proposed 5th Directive see Chapter 5.2. at pp. 198. Article 33 of the proposal states: "(1) *The shareholder's right to vote shall be proportionate to the fraction of the subscribed capital which the shares represent.*

(2) *Notwithstanding paragraph 1, the laws of the Member States may authorise the memorandum and the articles of association to allow restriction or exclusion of the right to vote in respect of shares which carry special pecuniary advantages. Such shares may not be issued for an amount exceeding 50 % of the subscribed capital. Where the company has not fulfilled the obligations arising in respect of such shares for a period which may not exceed three consecutive accounting years, the holders of those shares shall acquire voting rights in proportion to the fraction of the subscribed capital which those shares represent, and the voting rights thus acquired shall be equivalent to those of the other shareholders.*"

3.3.2. Proxy Voting

According to section 372 (1) of the Companies Act 1985 every shareholder is entitled to appoint a person, his proxy, to vote for him at a general meeting.²⁴² Proxy voting is a common feature in corporate practice in Britain.²⁴³ In most cases, directors are appointed as proxies. Having in mind that English company law allows directors to solicit proxies at the expense of the company on behalf of their policies, this is not surprising.²⁴⁴ It should also be borne in mind that the directors often hold substantial stakes in the company in their own right. Proxy votes in addition to own shares held by the directors can, of course, not only affect the balance of power between ownership and control in a company in favour of the directors, but also hamper a bid launched by an unwelcome bidder in a number of ways. Since directors are only entitled to take (massive) defensive action if the shareholders' approval is obtained,²⁴⁵ the directors could use their proxy-votes in order to empower themselves to take defensive measures against the bidder. Bearing in mind that in a takeover situation the entrenched management is usually threatened with losing their jobs it is obvious that a conflict of interest may arise.

Yet, this account may sound worse than the practical situation is. Since the shareholders are known by name in Britain²⁴⁶ the offeror can, for example, approach the shareholders directly and acquire

242 Reg. 59 Table A: "*On a poll votes may be given either personally or by proxy.*" Reg. 60 and 61 Table A set out sample forms for an instrument appointing a proxy.

243 *Dine*, European Company Law, para 15.18; *Boyle*, Barriers to Contested Takeovers in the EC, Company Lawyer, Vol. 12, No. 9, p. 163, 165 (1991).

244 *Peel v. London and North Western Railway Co* [1907] 1 Ch 5. See also *Dine*, European Company Law, para 15.17.

245 General Principle 7 and Rule 21 of the City Code.

246 Section 352 of the Companies Act 1985 requires a company to maintain a register of members in which the name, address and the number of shares held by the shareholder must be stated.

proxies for itself.²⁴⁷ Furthermore, a large number of the shares in a listed company is normally held by institutional investors²⁴⁸ who do not normally appoint proxies and whose paramount interest usually is to generate maximum profits and not to support any particular management.

Nevertheless, restrictions on the use of proxies are contained in the proposed Fifth Directive.²⁴⁹ Most importantly, Article 28 provides that in principle the appointment of a proxy shall be for one meeting only (unless a second meeting has the same agenda) and requires, inter alia, the proxy holder to request instructions from the shareholder concerning the exercise of his voting rights.

The problem of proxy voting has a different dimension in Germany where bearer shares are used and banks²⁵⁰ are appointed as proxies. The role of the banks in Germany will be discussed in detail in Chapter 4.2.3.²⁵¹

3.3.3. Cross Shareholdings

Cross shareholdings - both nationally and internationally - are a feature of any modern economy.²⁵² Most of these stakes are held for genuine investment reasons. However, mutually supportive holdings can also be used by the incumbent directors of two or more companies acting together to increase their influence and make their

247 *Prentice*, Regulation of Takeover bids, p. 152.

248 Institutional shareholders control about two-thirds of U.K. equities according to the *Trade and Industry Committee Report on Takeovers and Mergers*, 1991, para 210.

249 See in detail Chapter 5.2.3. at pp. 201.

250 It is also common for British banks and investment funds to hold their clients' shares in named accounts and vote those shares. See *Boyle*, *Barriers to Contested Takeovers in the EC*, *Company Lawyer*, Vol. 12, No. 9, p. 163, 165 (1991).

251 See Chapter 4.2.3. at pp. 143.

252 *Boyle*, *Barriers to Contested Takeovers in the EC*, *Company Lawyer*, Vol. 12, No. 9, p. 163, 165 (1991); *Dine*, *EC Company Law*, para 15.20.

companies - and their own jobs - immune against takeover bids and, thus, affect the balance of power between management and shareholder control.²⁵³ Furthermore, from an economic point of view, any cross holding amounts ultimately to holding a stake in the own company which runs counter to the concept of capital maintenance and, hence, puts creditors potentially at risk.²⁵⁴

Although the harmful effect of cross shareholdings is clearly visible, only few rules exist in English law to deal with this problem. The only provision that deals directly with the question is section 23 (1) of the Companies Act 1985 which prohibits a subsidiary from holding shares in its holding company, the latter being defined as a company which holds the majority, i.e. more than 50 per cent, of the voting rights of the other company.²⁵⁵ To a limited extent cross shareholdings are impeded by the Stock Exchange's Yellow Book which provides that - normally²⁵⁶ - at least 25 per cent of any class of listed shares must be in the hands of the public, i.e. persons who are not associated with the directors or major shareholders.²⁵⁷ This particular provision of the Yellow Book originates from the *Admissions Directive*.²⁵⁸ Not directly addressing the problem of cross shareholdings, but also having a somewhat adverse effect is Rule 9 of the City Code which requires a mandatory offer to be made once the 30 per cent threshold is exceeded. By this means cross holdings have to remain below 30 per cent. However, mutual holdings below this threshold are not restricted.

Under the present rules, many different structures of cross shareholdings designed to prevent a takeover are possible.²⁵⁹ A

253 *Weinberg/Blank*, Takeovers, para 3-781 et seq.

254 *Emmerich/Sonnenschein*, Konzernrecht, § 5 II 1.

255 Section 736 CA 1985.

256 A lower percentage of shares distributed to the public may be allowed by the Stock Exchange if it is considered that the market will nevertheless operate properly; para 3.19 of the Yellow Book.

257 Para 3.18 of the Yellow Book.

258 Admissions Directive, No. 79/279/EEC of 5 March 1979, [1979] O.J. L 66/21.

259 *Weinberg/Blank*, Takeovers, para 3-781.

fairly simple but nevertheless effective structure would be where three companies with co-operating boards hold stakes of 26 per cent in each other. In this kind of situation, neither company would be the holding company of any other nor has any of them exceeded the 30 per cent threshold. Nevertheless, any two companies together would hold the majority in the third company and could therefore prevent any hostile takeover bid. However, if the parties entered into a formal agreement or their co-operation were very intensive, the Panel would regard them as shareholders acting in concert and the obligation to make a mandatory offer would arise.²⁶⁰ It appears doubtful, however, whether the Panel could detect informal agreements of that kind since it seems almost impossible to determine in practice whether an investment is made for genuine or improper, namely defensive, reasons.

This difficulty might also be the reason why there has not been effective legislation against mutually supportive holdings. Furthermore, any legislation designed to restrict cross holdings other than prohibit them entirely would necessarily be very complex and complicated. This last point is especially well demonstrated by the German piece of legislation which attempts to tackle harmful cross shareholdings.²⁶¹ The problem of cross shareholdings is - probably for the same reasons - also not addressed in the proposed Fifth Directive or, indeed, any other Directive²⁶².

260 As to "*acting in concert*" see City Code, Definitions.

261 See Chapter 4.3.3. at pp. 164.

262 *Dine*, EC Company Law, para 15.22.

3.3.4. Increase of Capital or Issue of Shares to a supportive Holder

The directors may, if authorized by the articles, increase the company's share capital by an allotment of equity shares, the basic effect of which is to make an offer more expensive to a potential bidder.²⁶³ If a potential bidder has already built up a stake in the target company he could, however, benefit from an allotment of equity shares for cash by way of exercising his normally existing pre-emption rights.²⁶⁴ For a board intending to protect the company or themselves against a takeover bid it would be most effective therefore to disapplicate the pre-emption rights and issue the shares to a friendly holder, thus, creating a situation comparable to a cross holding. This, however, seems quite impracticable for a listed public company, both for legal and factual reasons.

Legally, since the coming into force of the Companies Act 1980 a number of statutory provisions, now to be found in the 1985 Act, exist in addition to the common law fiduciary duties of directors. Section 80 of the Companies Act 1985 stipulates that directors may only allot shares if they are authorised to do so either by an ordinary resolution in the general meeting or the company's articles. Further and more stringent requirements are to be met to disapplicate pre-emption rights.²⁶⁵ Pre-emption rights may only be excluded if the directors are generally authorised by the articles - as opposed to an authorisation by an ordinary resolution - to allot shares. If so, the pre-emption rights may be disapplicated by either a provision in the articles or a special resolution.²⁶⁶ But even where the directors are empowered by the articles to allot shares without being bound by

263 Reg. 32 of Table A; section 80 et seq.

264 Section 89 CA 1985.

265 Section 95 CA 1985.

266 As to further requirements regarding the special resolution see section 95 (5) CA 1985.

pre-emption rights, they still have to comply with their fiduciary duties which require them to act in what they consider the best interests of the company and for a proper purpose. Quite a number of significant cases dealt with the very situation that the directors issued shares to influence the outcome of a bid in one way or another.²⁶⁷ In broad terms, the essence of these decisions may be summarized by saying that the desire to frustrate a hostile offer in order to remain in office must not be the only motivation for the issue of new shares. In other words, where the issue of shares can be justified objectively by some proper management considerations, the directors act within the scope of their power.²⁶⁸ In addition to these legal requirements applying to all public companies, listed companies must comply with the numerous provisions of the Stock Exchange's Yellow Book²⁶⁹ which requires a company intending to issue equity shares, irrespective of what is stipulated in the articles, to obtain shareholder consent if pre-emption rights are to be disapplied.²⁷⁰

Since an issue of fresh shares is often on profitable terms and a disapplication of pre-emption rights would tend to dilute the existing shareholders' stakes, the shareholder consent concerning the disapplication will not normally be given by institutional investors. They even have announced that they will not support disapplication in listed companies unless the disapplication relates to not more than 5 per cent of the equity shares.²⁷¹ Together with the mentioned legal restrictions it seems nowadays therefore most unlikely that a listed company may successfully issue shares to a friendly holder in order to frustrate a future takeover bid. In addition, once a bid has been

267 Re Smith & Fawcett Ltd. [1942] Ch. 304; Hogg v. Cramphorn [1967] Ch. 254; Smith Ltd. v. Ampol Petroleum Ltd. [1974] A.C. 821; Pine Vale Investments v. McDonnal and East Ltd. (1983) 8 A.C.L.R. 199; Whitehouse v. Carlton Hotel Ltd. (1987) 70 A.L.R. 251; McGuire v. Ralph McKay Ltd. (1987) 12 A.C.L.R. 107.

268 See in particular the Privy Council decision Smith Ltd. v. Ampol Petroleum Ltd. [1974] A.C. 821. Also *Xuereb*, *The Rights of Shareholders*, p. 62.

269 See Chapter 4 of the Yellow Book.

270 Para 4.42 of the Yellow Book.

271 *Keenan*, *Company Law*, p. 195.

communicated, the very stringent restrictions of the City Code apply which explicitly state in Rule 21 (a) that the directors must not issue any authorised but unissued shares without the shareholders' consent.²⁷²

3.3.5. Compensation Packages for Directors

Unlike many other European countries, the removal of directors as such does not constitute a barrier to takeover bids in Britain.²⁷³ On the contrary, because of the single-tier board system together with section 303 of the Companies Act 1985, which provides that a company may remove a director "*by ordinary resolution before the expiration of his period of office, notwithstanding anything in its articles or in any agreement between it and him*", the removal of directors appears rather facile. However, section 303 (5) of the 1985 Act makes also clear that a director so removed is not deprived of his right to claim damages for breach of a contract of or for services. Hence, long term service agreements between the directors and the company will lead to substantial financial compensation claims if the directors of the target board are replaced in the aftermath of a takeover as is often the case. This might make the target company at least less attractive to a potential bidder.

Regulation 82 of Table A of the 1985 Companies Act vests the power to determine the directors' remuneration in the general meeting (ordinary resolution). Such a provision in the articles does, however, not constitute a contract between the directors and the company.²⁷⁴ Therefore, directors usually enter into a service or

272 See Chapter 3.1.1.(2)(d) at pp. 35, and Chapter 3.4 at pp. 85.

273 But see the above discussion of *Bushell v. Faith* [1969] 1 All ER 1003 at Chapter 3.3.1. at p. 71. As to the removal of the management under German law see Chapter 4.2.2.(1)(b) at p. 136, and Chapter 4.2.2.(2)(a) at p. 137.

274 *Palmer's Company Law*, para 8.038.

employment contract with the company. Thereby the company is represented by board as Regulation 84 of Table A makes clear: “... *the directors may appoint one or more of their number and enter into an agreement or arrangement with any director for his employment by the company...*” Concerning the terms of that contract the directors are according to Regulation 84 of Table A largely free: “... *Any such appointment , agreement or arrangement may be made upon such terms as the directors determine and they may remunerate any such director for his services as they think fit.*” The fact that the directors in negotiating their contracts basically contract with themselves gives rise to concern as there clearly is a potential for a conflict of interest. The German two-tier board system avoids this problem to a large extent: Concerning employment contracts of management board members, the company is represented by the supervisory board. The supervisory board determines the salary of the management board members, which according to the Stock Corporations Act has to be adequate and must not be excessive.²⁷⁵ The remuneration of the supervisory board members, which also has to be “reasonable”, is either determined by the articles or by a resolution of the general meeting.²⁷⁶

In order to prevent abuses by directors in respect of their remuneration the British Companies Act 1985 contains a number of provisions dealing with directors’ service contracts. Most notably, section 319 stipulates that any contract of employment of a director for a period of more than five years must be approved by the shareholders in general meeting. The *Cadbury Report* on “*The Financial Aspects of Corporate Governance*” is even more restrictive and recommends that executive director’s service contracts should not exceed three years unless shareholder approval is obtained.²⁷⁷

275 Sec. 87 AktG.

276 Sec. 113 AktG.

277 *Finch*, Corporate governance and Cadbury: self-regulation and alternatives, [1994] J.B.L. 51, 53.

Furthermore, section 312 requires disclosure and shareholder approval for any payment by way of compensation for loss of office. As section 316 (3) points out, however, the requirement of disclosure and shareholder approval does not apply in so far as a "*bona fide payment by way of damages for breach of contract or as consideration for or in connection with his retirement from office*" is concerned²⁷⁸ or where the company is contractually obliged to make a certain payment.²⁷⁹ Section 318 requires companies to keep the particulars of their directors' service contracts which run longer than one year open to inspection by any shareholder without charge at the company's registered office. Similar provisions are contained in the Stock Exchange's Yellow Book.²⁸⁰ A potential bidder holding at least one share can therefore easily ascertain the amount of damages it is liable to pay after removing the directors in the wake of a successful bid. Detailed information - specified in Schedule 6 of the Companies Act 1985 - regarding the emoluments and other benefits of directors must also be disclosed in the notes to a company's annual accounts. This too may prove helpful in assessing potential damages payable to the target directors.

In addition to these requirements, the City Code stipulates in Rule 25 (4) that the first major circular from the offeree board advising shareholders on an offer must contain particulars of all service contracts of the directors if these contracts have more than one year to run. Furthermore, Rule 21 prohibits the offeree board directors from entering into contracts otherwise than in the ordinary course of business without shareholder consent when a bona fide offer is made or imminent. Note 6 makes clear that any "*abnormal increase in the emoluments or a significant improvement in the terms of service*" in the directors' contracts would in a bid situation be

278 *Palmer's Company Law*, para 8.214.

279 *Taupo Totara Timber Co. Ltd. v. Rowe* [1978] A.C. 537.

280 Paras 16.9 to 16.12 of the Yellow Book.

considered out of the "*ordinary course of business*", i.e. an inadmissible defence.

Although the legal and quasi-legal environment regarding "*golden handshakes*" is rather restrictive, a method commonly used to increase the compensation payable in case of a director's removal is the so called "*rolling contract*".²⁸¹ These service contracts of directors contain a term which renews the contract every day for a certain period. In accordance with the *Cadbury Report*, three years rolling contracts are most common.²⁸² Hence, the directors' contracts keep "rolling" the effect of which is that in case of dismissal at any given time the service contract always has the full period until expiry, thus, where a three-years contract is concerned, three more years to run. The dismissed director is consequently entitled to compensation for the loss of a three-year service contract, i.e. three times his annual salary plus bonuses and pension arrangements. A recent survey revealed that among the FT-SE 100 companies about 50 per cent of the chief executives were on three-year rolling contracts.²⁸³ However, criticism against three-year contracts from institutional investors is increasing. In the current political climate where so-called "*boardroom greed*" is widely discussed and was looked into by the House of Commons Employment Committee as well as the private Greenbury Committee²⁸⁴ the future of the three-year rolling contracts looks gloomy. The chief executive of the £25 billion *PosTel* pension fund, Ross Gooby, has already announced

281 *Times*, 18 October 1994.

282 As to the Cadbury Report: *Finch*, Corporate governance and Cadbury: self-regulation and alternatives, [1994] J.B.L. 51, 53.

283 Bacon & Woodrow's 1994 Directors' Total Remuneration Package Survey. Among the 100 FT-SE 100 companies only 80 replied. In 39 per cent of all companies surveyed the Directors are on three-year contracts. The average basic income of chief executive directors in July 1994 was £208,000. Further details in *Times*, 18 October 1994.

284 Chaired by Sir Richard Greenbury, the £689,000 chairman of Marks & Spencer. See *Times*, 7 March, 19 April and 17 July 1995. The Greenbury Report suggests to set service contract periods at one year or less. As to the contrary view see the interesting remarks by Rees-Mogg, Busybodies are bad for business, *Times*, July 17, 1995.

that *PosTel* would in future vote against directors' service contracts of more than two years.²⁸⁵

According to a survey conducted by a corporate governance consultancy, *Pirc*, U.K. companies have paid out more than £65 million in compensation to directors who have resigned or accepted less favourable terms in the past three years.²⁸⁶ A recent example for the dimension of a director's compensation for loss of office in the context of a takeover is the case of *John Robb*, former chairman and chief executive of *Wellcome*, who had to resign after his company was taken over by *Glaxo* early in 1995. Being only on a two year rolling contract his basic compensation amounted to twice his annual salary of £475,000, i.e. £950,000. In addition, shares and share options netted a further £1,300,000 which brought his "golden handshake" to well over £2 million.²⁸⁷ Needless to say, the other *Wellcome* directors enjoyed lucrative share options and employment contracts too.²⁸⁸ When *BET*, the business services group, after a £2.2 billion bid by *Rentokil* was taken over in spring 1996, the chief executive of *BET*, *Mr John Clark*, made a profit of £3.4 million from selling shares as a result of the bid plus, being on a three year rolling contract of about £415,000 annually, more than £1 million in compensation for loss of office.²⁸⁹ In addition, in a court battle he is seeking more than £4 million in damages for lost benefits such as bonus payments, share options and pension entitlements.²⁹⁰

285 *Times*, 18 October 1994. A recent survey by the consultancy *Pirc* has, however, revealed that the recommendations of the 1995 Greenbury report have been ignored by many quoted companies: "We're pointing out that any recommendations that involve taking mone out of executives' wallets have been ignored." See *Financial Times*, 16 October 1996.

286 *Financial Times*, 16 October 1996.

287 *Times*, 16 February 1995 and *Times*, 24 March 1995. *John Robb* had options over 250,756 shares and a further 13,750 shares according to the *Times*, 31 January 1995.

288 *Times*, 31 January 1995.

289 *Financial Times*, *BET* chief poised to net £5m in takeover aftermath, 11/12 May 1996.

290 *Financial Times*, 14 October 1996 and 16 October 1996. This case is particularly interesting because it is expected to establish whether

But however huge - and in many cases probably undeserved - these sums may seem for any individual to receive, it remains doubtful whether large compensation packages really constitute a serious barrier to takeovers of listed companies. In the context of the enormous sums involved in making such a bid - about £9 billion in the mentioned *Glaxo/Wellcome* battle - a couple of million pounds for the "boys" at the target's board may seem "peanuts" for any serious bidder. Moreover, the bidder's board might find itself in the same position some day and has, naturally, therefore little interest to oppose this system for which the shareholders pay the bill.

3.4. Defences against an existing Offer

In any legal system in which directors are authorised to take defensive actions against takeover bids this represents a serious barrier to the market for corporate control, and it is an undisputed fact that, even if defensive actions do not actually defeat the bid, they increase the takeover costs substantially.²⁹¹ As far as Britain is concerned it has been pointed out earlier that one of the City Code's fundamentals, stated in General Principle 7 and further specified in Rule 21, is to prevent the target board from taking any frustrating action after a bona fide offer has been communicated or the target board has reason to believe that a bona fide offer might be imminent,

compensation should relate solely to loss of salary or whether share schemes and bonus arrangements should be included.

291 *Weinberg/Blank*, Takeover, para 1-011 and 3-833. For practical examples see *Times*, 11 January 1995: Trafalgar faces £60 million bid fees. *Financial Times*, 8 March 1995: the *Glaxo/Wellcome* bid expenses were expected to be around £100 million. *Glaxo*, advised by *Lazard Brothers*, had estimated its expenses at £77 million, of which £30 million were fees, and the rest stamp duty. *Wellcome*, advised by *Barings* and *Morgan Stanley*, was expected to pay between £20 and £30 million. See also *Financial Times*, 24 January 1996: the *Granada/Forte* battle incurred £140 million in fees and costs. See also *Guardian*, 30 January 1995: Merger mania is madness.

except with the shareholders's consent.²⁹² Additionally, the Code provides in General Principle 9 that the directors must only have regard to "*the shareholders's interests taken as a whole, together with those of employees and creditors*" and not to their personal interests. From the wording of these provisions it appears, thus, that the hands of the directors are rather strictly bound. There are, however, a number of "adverse" actions left which are either tolerated by the Panel or not considered a defence in the strict sense of the Code. Since the possible measures are quite numerous a choice had to be made and the following expositions do not intend to be exhaustive, but try to highlight the most common defence tactics.

3.4.1. Lobbying Shareholders

To lobby for shareholder support seems an obvious line to take for an entrenched board struggling to fend off a bid. Again, both the City Code and common law limit the directors' freedom of action.

According to General Principle 5 of the City Code "*any document or advertisement addressed to shareholders containing information or advice ... must be prepared with the highest standards of care and accuracy.*" A number of Rules concretise this principle further.²⁹³ As far as common law duties are concerned directors usually owe their fiduciary duties only to the company.²⁹⁴ However, it follows from *Gething v. Kilner* that directors in the context of a takeover also owe

292 See Chapter 3.1.1.(2)(d) at p. 35.

293 Rule 19: Standards of care in respect of information;
Rule 23: The general obligation as to information;
Rule 25: Offeree board circulars;
Rule 28: Profit forecasts;
Rule 29: Asset valuations.

294 *Percival v. Wright* [1902] Ch. 421. See also section 309 (2) CA 1985.

a duty to their shareholders to be honest and not to mislead them by suppressing information.²⁹⁵

Within these boundaries, directors may try to win their shareholders' support with a number of arguments. A likely line of defence in any takeover battle is to argue that the bid undervalues the target company, i.e. that the offer is inadequate and shareholders should receive a higher offer or keep their shares. This course was, for example, chosen by the *Wellcome* board to defend against the *Glaxo* bid. Apart from circulars and personal talks to major shareholders, advertisements - such as the one shown at page 89 - appeared for a number of days in various national newspapers asking the shareholders to call to hear the *Wellcome*-board's advice. By calling one could hear a recorded message from *John Robb*, the former chairman and chief executive of *Wellcome*, explaining in some detail why the board thought the *Glaxo* bid undervalued *Wellcome* and that the board were trying to solicit a better offer from another company, thus, asking the shareholders not to make any commitments.

Another line of argument is to criticise the bidder. An example of this approach could recently be witnessed in the case of *Northern Electric's* defence against the *Trafalgar House* bid where the question was raised whether a company - *Trafalgar House* - which had not always complied with the *Cadbury Code* was good enough to run a public utility.²⁹⁶ The complicated corporate structure of *Trafalgar House* with its Hong Kong and Bermuda based ownership²⁹⁷, its poor economic record in the last few years and its inexperience in the field of electricity generation had also been stressed.

295 *Gething v. Kilner* [1972] 1 All ER 1166.

296 *Times*, 24 January 1995.

297 *Times*, 14 and 24 January 1995.

Given the fact, however, that shareholders normally put their financial interests first all lobbying will be fruitless if the offer price is right.²⁹⁸ This kind of defence therefore appears quite harmless.

²⁹⁸ As to appeals to loyalty and patriotism see *Weinberg/Blank*, Takeovers, para 3-825.



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3.4.2. Increased Dividends

A more serious defence is the promise of higher dividends or other financial incentives by the target board in order to keep - or rather buy - their shareholders' loyalty. Albeit Note 3 to Rule 21 of the City Code states that the "*payment of an interim dividend by the offeree company ... may in certain circumstances be contrary to General Principle 7 and this Rule in that it could effectively frustrate an offer*" and the directors are further bound by their fiduciary duties and some statutory provisions²⁹⁹ it appears that they do enjoy quite some leeway. For instance, in *Trafalgar's* bid for *Northern Electric* the entrenched management came up with an amazing package of incentives designed to "bribe" their shareholders as the *Times* put it.³⁰⁰ This included a £1.50 one-off dividend per share, the issue of £111 million worth of unredeemable new preference shares, worth at least £1 per share, and an announcement that *Northern's* holding in the *National Grid* would be handed over directly to its shareholders, which would have been worth a further £2.57 per share. In aggregate, the incentive package would have been worth more than £5 per share.³⁰¹ The overall cost of the proposed incentive package amounted to almost half the bid price (!) and consequently led to critical questions as to the price control mechanism in the electricity industry. Following this, an announcement to review price controls by the power regulator, *Professor Littlechild*, caused a dramatic slump in the value of all electricity shares, which, broadly speaking, led to the eventual failure of *Trafalgar's* bid.³⁰² In view of these facts, one has to admit that *Northern's* directors built up an impressive defence astonishing all City pundits. It is more than doubtful, however,

299 Sections 263 (1) and 264 (1) CA 1985 which basically stipulate that distribution shall not be made except out of profits.

300 *Times*, 24 January 1995 (Pennington).

301 *Times*, 18 and 25 February 1995.

302 *Times*, 11 and 16 March 1995; *Financial Times*, 8 March 1995.

whether these enormous handouts to shareholders could have been justified with any genuine business reasons. Given these facts, it appears equally doubtful whether the chief motivation of the directors was to act in the interest of the company as a whole as their fiduciary duty requires rather than defend their own positions. As far as the City Code is concerned, it is beyond question that they did neither act in accordance with the spirit of the Code to refrain from taking any actions designed to frustrate a bona fide offer³⁰³ nor with its wording.³⁰⁴ The amazing thing is, however, they seemed to get away with it without any apparent intervention by the Panel.

3.4.3. Lobbying the Merger Control Authorities

Representations to the competition policy authorities to persuade them to veto the merger have always been a defence strategy in Britain.³⁰⁵ As Part Three of this work analyses the merger control systems in Britain,³⁰⁶ Germany³⁰⁷ and under the European Merger Regulation³⁰⁸ in more detail, a few broad remarks as to the role of lobbying in the merger control process may suffice at this stage.

If a bid is referred to the Monopolies and Mergers Commission (MMC), it lapses automatically.³⁰⁹ Bearing in mind the City Code's wording in General Principle 7 that no frustrating action may be taken by the board of the offeree company, the question has been

303 General Principle 7.

304 Rule 21, esp. Note 3.

305 As to the topic in general see Lofthouse, *Competition Policies as Takeover Defences*, [1984] J.B.L. 320 and *Weinberg/Blank*, *Takeovers*, para 3-831 et seq.

306 See Chapter 6, at p. 265.

307 See Chapter 7, at p. 335.

308 See Chapter 8, at p. 391.

309 Rule 12 (a) of the City Code. An interesting report on how the lobbying process works (BAe/GEC/VSEL) in practice gives *Gray*, *A resounding pitter-patter of political arm twisters*, in the *Financial Times*, 9 November 1994.

raised whether lobbying is prohibited by the Code.³¹⁰ Although instigating a court procedure is considered inadmissible, the Panel took the view that lobbying is a democratic right which must be allowed.³¹¹ The main difference between litigation on the one hand and lobbying merger authorities on the other seems to be that court proceedings are conducted in the (private) interest of the plaintiff whereas merger policy is exercised objectively in the public interest. Furthermore, section 76 (2) of the Fair Trading Act 1973 now provides that representations made to the Director General of the Office of Fair Trading (OFT) by interested parties are to be taken into account.³¹² Hence, lobbying is not so much seen as exercising undue influence over the merger control authorities, but helping to bring arguments forward, or, as *Finbow/Parr* put it, “*the art of educating government - of seeking to ensure that the OFT, the MMC and the Secretary of State together have available as much relevant information as possible to enable them to reach an informed decision on the issues raised by the merger.*”³¹³ Lobbying the merger control authorities can therefore not be illegal. Yet, it has been argued by one author that the defending directors might contravene against their fiduciary duty to act in the best interests of the company by lobbying the merger control authorities since a merger would normally reduce competition which is generally good for the company involved in terms of higher profits.³¹⁴ However, in view of

310 *Lofthouse*, Competition Policies as Takeover Defences, [1984] J.B.L. 320, 329.

311 Panel statement on Hoylake Investments/BAT Industries plc, September 6, 1989: see *Morse*, The City Code, multinationals and overseas regulatory procedures, adaptation or surrender?, [1990] J.B.L. 67.

312 Section 76 (2) which was added by the CA 1989. As to the discretion enjoyed by the Secretary of State see *R. v. Secretary of State for Trade and others, ex parte Anderson Strathclyde plc* [1983] 2 All ER 233, 242: “... he [the Secretary of State] is entitled to take into account all the relevant circumstances, and to consider the opinion of the minority of the commission, and also representations and advice from persons other than members of the commission.”

313 *Finbow/Parr*, U.K. Merger Control, p. 293.

314 *Lofthouse*, Competition Policies as Takeover Defences, [1984] J.B.L. 320, 323 et seq.

section 76 (2) of the Fair Trading Act 1973, this argument can hardly be sustained.

The reason why the merger control authorities are so frequently and intensely exposed to lobbying - which is not the case in Germany where lobbying the Federal Cartel Office in Berlin would for structural reasons probably be contraproductive³¹⁵ - lies in the relatively wide discretion they enjoy in the decision-making process,³¹⁶ the fact that the ultimate decision is made by a politician, namely the Secretary of State for Trade and Industry,³¹⁷ and also in the rather broad "*public interest*" criterion against which mergers are assessed in Britain compared to the rather narrowly defined "*market dominance*" criterion applied in Germany³¹⁸ and under the European Merger Regulation.³¹⁹ A recent example where intense lobbying took place and led to surprising decisions is the rival bid by *BAe* and *GEC* for the submarine maker *VSEL* which will be discussed at a later stage at page 230.³²⁰

In practice, however, the criteria taken into account by the merger control authorities are primarily competition aspects and it happens not often that a merger is referred or blocked on non-competition grounds.³²¹ Non-competition aspects which may have an effect are, for example, employment issues and the fact that the bidder is a foreign state-owned and controlled company.³²² The fact

315 See Chapter 7.4.1.(3) at p. 307.

316 As to the discretionary nature of the British merger control process see Chapter 6.1.2. at pp. 268; Chapter 6.3.2. at pp. 293, and Chapter 6.3.4. at pp. .

317 See in further detail Chapter 6.3.4. at pp. 242. See also *Sir Bryan Carsberg's* remarks reported in the *Times*, 23 February 1995. Also *Begg*, *Corporate Acquisitions*, para 8.39: "*Merger Control in the United Kingdom is a highly discretionary affair*" and constitutes, in the words of the *Financial Times*, "*one of the most visible and arbitrary forms of ministerial intervention.*"

318 See Chapter 7.5. at pp. 386.

319 See Chapter 8.4. at pp. 377.

320 As to the lobbying taking place see *Gray*, A resounding pitter-patter of political arm twisters, in the *Financial Times*, 9 November 1994. The case is discussed in Chapter 6.3.2. at p. 230.

321 For a detailed analysis see Chapter 6.4. at pp. 304.

322 See Chapter 6.4.2. at pp. 311.

of foreign ownership alone, however, has apparently never been the reason for a MMC reference or the blocking of a bid.³²³ Section 13 of the Industry Act 1975 which provides that a prohibition order may be issued by the Secretary of State where the change of control in an "*important manufacturing undertaking*" is considered contrary to the interests of the United Kingdom has also never been invoked.

Compared to the German system, where a merger is - broadly speaking - automatically blocked if certain criteria are met,³²⁴ the British system is more flexible on the one hand, but also less predictable and more open to political influence on the other hand as the further analysis in Chapters 6 and 7 will demonstrate. Thus, in the present context of takeover barriers it may be concluded that lobbying the merger control authorities may be used by the defending board members as means to influence the outcome of a bid. However, as lobbying in Britain is very much seen as "*educating government*" and does due to a different legal framework and culture apparently not have the negative tinge it has in Germany, it is a legitimate "defensive" measure neither infringing the fiduciary duties of the directors nor the rules of the City Code.

3.4.4. Search for a "White Knight"

In contrast to the defensive actions discussed above, the search by the target's directors for a rival bidder, the so-called white knight, to come up with a higher offer does not tend to deprive the shareholders of their right to decide upon the merits of the (first) offer. On the contrary, by creating an auction-like situation the shareholders get a wider choice and are likely to receive a higher price as a result. Thus, there is no reason for either the Code or the

323 See Chapter 6.4.2.(2) at pp. 258.

324 See Chapter 7.5. at pp. 386.

law to restrict this kind of activity of the directors. One might even argue that the directors required to act in the best interests of the company are obliged to look for an alternative bidder in order to push the price and boost the shareholders' profits.

In *Glaxo's* recent bid for *Wellcome*, for example, the latter is understood to have - unsuccessfully - approached *Hoechst* of Germany and the U.S. companies *Bristol-Myers-Squibb*, *Pfizer*, *Merck* and *Johnson & Johnson* in order to solicit a higher offer.³²⁵

Where competing bids exist³²⁶ the difficult question arises whether the directors are always obliged to support the highest bid. In *Heron International Ltd. v. Lord Grade* the Court of Appeal held that "*where directors have decided that it is in the best interest of a company that the company should be taken over and there are two or more bidders the only duty of directors, who have powers as those in Article 29*³²⁷ *is to obtain the best price. ... Where the directors must only decide between rival bidders the interests of the company must be the interests of the current shareholders.*"³²⁸ Hoffmann J. in *Re A Company*, however, took a different view by saying: "*I cannot accept the proposition that the board must inevitably be under a positive duty to recommend and take all steps within their power to facilitate whichever is the highest offer.*"³²⁹ At the root of this problem lies the question of how to define the interests of the company in accordance with which the directors have to act: Are the interests of the company synonymous with the interests of the current shareholders³³⁰ or do the directors have to take wider issues

325 *Times*, 31 January 1995 and 2 February 1995.

326 As to the competition implications of competing bids see Chapter 6.3.2. at p. 230.

327 Article 29 of the target company's articles of association provided that any transfer of shares required the directors' approval.

328 *Heron International Ltd. v. Lord Grade* [1983] BCLC 244, 265. Article 29 of the companies articles of association provided that any transfer of shares required the directors' approval.

329 *Re A Company* [1986] BCLC 382, 389.

330 So *Weinberg/Blank*, Takeovers, para 3-835; *Heron International Ltd. v. Lord Grade* [1983] BCLC 244.

into account? As section 46 (1) of the Companies Act 1980 already did, section 309 (1) of the Companies Act 1985 stipulates that the directors have to have regard to the interests of the employees and not only to the shareholders' interests.³³¹ The effect of this provision is somewhat diluted, however, by subsection (2) which states that this duty is owed only to the company and not to the employees. This means in practice that the employees have no right to sue for breach of duties so that there is no effective enforcement of section 309. However, section 309 may well be used by directors to justify a decision which seems to contravene the current shareholders' interests. Whether the interests of "future" shareholders are to be taken into account is a controversial question in English company law, although this idea is opposed by the majority opinion since "future" shareholders cannot be identified and have no current interest in the company.³³²

General Principle 9 of the City Code adopts an even wider view than section 309 by stating: *"It is the shareholders' interests taken as a whole, together with those of employees and creditors, which should be considered when the directors are giving advice to shareholders."* Albeit this does not imply that the interests of "future" shareholders are to be considered, under the Code the directors must have regard to far more aspects than just the satisfaction of the present shareholders. Interestingly, the predecessor of General Principle 9, then General Principle 11, dealt expressly with the situation of directors recommending a lower bid by providing: *"There may be good reasons for such a board³³³ rejecting an offer or preferring the lower of two offers. The board must carefully examine*

331 Section 46 (1) CA 1980 and section 309 (1) CA 1985 have the same wording: "The matters to which the directors shall have regard in the performance of their functions shall include the interests of the company's employees in general as well as the interests of its members."

332 In the Savoy Hotel case, counsel had advised the directors that they should pay regard to the interests of "present and future members of the company." See *Weinberg/Blank*, Takeover, para 3-835 with further references.

333 Refers to companies which are effectively controlled by their directors.

its reasons for doing so and be prepared to explain its decision to its shareholders."

In terms of recommending a bid, it seems therefore that the directors are free - in accordance with both the law and the Code - to support a lower bid if they have proper reasons to do so,³³⁴ and in that way defend against an unwelcome higher offer.

3.5. Concluding Remarks

Evaluating takeover regulation and barriers in Britain, it seems useful to differentiate between the substance of the rules governing takeovers on the one hand and the institutional framework established to administer and enforce these rules on the other hand.

The essence of the of the British takeover rules is laid down in the General Principles of the City Code, of which equal treatment, adequate information of shareholders, transparency in dealings, and the restriction on frustrating action are the most substantial tenets. Regarding the fundamental values of the City Code there is very little to say in terms of criticism and it is deservedly seen as a model for a future European regulation. Its rules are neutral in the sense that neither the bidder nor the target company is treated favourably. The mandatory bid rule - often heavily criticized in Germany in connection with the previous proposals for a European Takeover Directive³³⁵ - appears to work very well in Britain. The German argument that such a rule would unduly hinder share transactions is largely refuted by

334 The opposite view takes *Weinberg/Blank*, Takeovers, para 3-385. As to the legal problem how far so called lock-out agreements between a target board and a bidder are binding see *Crowther Group plc. v. Carpets International plc* [1990] BCLC 560; *Dawson International plc v. Coats Patons* [1991] B.C.C. 278. For a thorough analysis see *Gower's Principles*, p. 711, 713. These kind of problems arose also in the *Glaxo/Wellcome* takeover: *Financial Times*, 8 March 1995.

335 See Chapter 5.1.1.(2) at pp. 177.

the British example. It is arguable, however, that too little regard is being paid to the employees of the target company by the Code. There is no rule granting the employees or their representatives a right to have either a say or at least to be informed by the offeror or the offeree or target board. Trade unions or other employee delegates are not represented on the Takeover Panel. As a takeover will in one way or another inevitably affect the employees of the target company, it would seem appropriate to ensure that the offer document is available to the employees since the bidder is obliged to state therein what its intentions regarding the business of the offeree company and its employees are³³⁶ and to give them a right to be informed by the board. The same holds true for the obligatory statement which has to be issued by the offeree board.³³⁷ In general, employee participation plays a much greater role in Germany as the following chapter will demonstrate.³³⁸

As to the institutional framework established to administer and enforce the takeover rules, the main responsibility lies with the Panel although the SROs as well as the Stock Exchange are also essential to the functioning of the whole system. The enforcement of the City Code works rather well due to the “City-style” network within which the Panel operates. Although the City Code is self-regulatory in nature, it is very much embedded in the regulatory structure established under the Financial Services Act 1986, in particular with respect to the enforcement of its rules. The commonly used phrase that takeover regulation in Britain is self-regulatory is therefore only partly true. Without the (enforcement) backing of the SIB, the various SROs and the Stock Exchange, all of which are statutory based institutions with statutory powers, the Panel would clearly not have the immense power it now enjoys.

336 Rule 24.1 of the City Code.

337 Rule 25.2 of the City Code.

338 See in particular Chapter 4.2.2.(2) at pp. 137.

Critically, it has been pointed out that the composition of the Panel³³⁹ and its attitude towards the influential merchant banks³⁴⁰ gives rise to concern as there must be a certain potential for conflict of interest.³⁴¹ It has also been questioned whether the very restrictive approach as to judicial review is adequate.³⁴² The *de facto* uncontrolled power enjoyed by the Panel is amazing and has certainly no parallel in Germany. Concerning this last point, however, it has to be admitted that the approach chosen by *Lord Donaldson* in restricting judicial review effectively rules out tactical litigation as a defence.

It is doubted, however, whether the institutional mainly self-regulatory framework which works apparently well for Britain can be seen as a model for other European countries, in particular Germany, or for a European Directive. The complex network within which the Panel operates is very much part of the close-knit, gentlemanly and maybe somewhat exclusive City-culture which used to be a unique feature of London as a financial centre. Yet, such a system cannot easily be adopted by any other country, as it is not just based on well drafted rules, but very much an intrinsic manifestation of a certain business culture and understanding which has developed in almost four decades. However, as the financial sector is becoming increasingly international, the City has already become less of a gentlemanly club and will most certainly continue to do so. The result of this could in the long run well be that new challenges arise for the self-regulatory Panel, especially from foreign bidders against whom it is much more difficult to enforce the Code's rules as the *St. Piran* case illustrated.³⁴³ Time will tell whether the (basically) self-regulatory system survives the process of increasing

339 See Chapter 3.1.2.(1) at pp. 36.

340 See Chapter 3.1.2.(3) at pp. 44.

341 As to the background of the Panel and Executive members see Table 7 at p. 39 and Table 8 at pp. 40 respectively.

342 See Chapter 3.1.2.(4) at pp. 51.

343 [1980] J.B.L. 270, 358; see also *Re St. Piran Ltd.*, [1981] 3 All ER 270.

internationalization which will undoubtedly take place in the coming decades.

Chapter 4

Takeover Regulation and Barriers in Germany

The fact that the U.K. is a net acquirer of companies in Germany demonstrates that any barriers can be surmounted if the German side is willing to co-operate.¹ The picture, however, is quite different when it comes to non-agreed takeover bids for German stock corporations. In Germany, corporate control in a stock corporation normally changes behind closed doors, agreed by like-minded managers, bankers, and big investors in a rather secretive way. Public bids followed by spectacular takeover battles and accompanied by a great deal of media attention are extremely rare in Germany. In recent years there were only very few events which bear some remote resemblance to anglo-saxon style hostile bids for listed public companies.²

1 See Table 1 at p. 18.

2 "Hostile" bids for non-listed stock corporations or private companies, where the shares are often held by a family or some other defined group of persons, may happen more frequently. In May 1988, for example, Maxwell Communications Corporation made a "hostile" bid for Brockhaus AG which was rejected by the 40 members Brockhaus and Meyer families who held the majority of the shares. Since only a tiny number of shareholders are involved in these kind of takeovers they belong to a category different from the one discussed in this work and are in their nature rather negotiations taking place behind the scenes than public bids. As to the MCC/Brockhaus case see *DTI, Barriers to Takeovers*, Vol. 2, p. 45.

(1) Flick Brothers ./ . Feldmühle Nobel

In 1988 the brothers *Gert-Rudolf* and *Friedrich-Christian Flick*, influential German industrialists, pronounced shortly before a general meeting of *Feldmühle Nobel AG*, which was convened to introduce a 5 per cent voting right limitation,³ that they opposed the voting right restriction and intended to make an offer to all shareholders in order to buy 50 per cent of the voting shares at a premium price.⁴ This, however, was disapproved of by the management of *Feldmühle*. The share price rose sharply in the days following the *Flick* announcement and the *Flicks* quickly withdrew their offer.⁵ Rumours at that time suggested that the share price increase was partly due to massive purchases by the leading German bank, *Deutsche Bank*, in support of the *Feldmühle* management.⁶ Nevertheless, the *Flick's* continued secretly - and against their public assurances⁷ - to buy *Feldmühle* shares at the stock exchanges until they owned a stake of about 40 per cent. Since the few disclosure provisions then existing only required *companies* to disclose their interest if their holding exceeded 25 or 50 per cent, the *Flick's* who acted as private investors were under no obligation to disclose their acquisitions.⁸ But for some reason having lost interest in controlling *Feldmühle*, they then sold their stake for a considerable premium to *Veba AG* in 1989, which brought *Veba's* holding to 46 per cent.⁹ The main significance of these events - apart from once again exposing the weakness of the German disclosure provisions¹⁰ - lies in the fact that for the first time somebody actually tried to take over a company

3 As to voting rights limitations in Germany see 4.3.1.

4 *Burgard*, Die Offenlegung von Beteiligungen, AG 1992, 41.

5 *Frankfurter Allgemeine Zeitung*, 13 and 14 June 1988.

6 *Frankfurter Allgemeine Zeitung*, 2 July 1988.

7 *Handelsblatt*, 30.6.1988; *Burgard*, Die Offenlegung von Beteiligungen, AG 1992, 41.

8 Sec. 20 AktG. For details see 4.1.2.(1) at pp. 123.

9 *Frankfurter Allgemeine Zeitung*, 16 August 1989.

10 *Burgard*, Die Offenlegung von Beteiligungen, AG 1992, 41.

against the resistance of its management. However, one has to admit that the similarity between a U.K. style hostile bid and the *Feldmühle* case is quite dim.

(2) *Pirelli* ./ *Continental*

The second case involved the Italian tyre manufacturer *Pirelli* who tried in 1990/1991 to win control over *Continental AG* in order to achieve synergic effects in the feeble European tyre business.¹¹ *Pirelli* approached *Continental's* management in September 1990.¹² Although *Continental* maintained that this approach had come as a big surprise, they promised to consider its merits,¹³ but finally rejected it. They argued a merger would not be in the interests of the company, its employees, shareholders, and its customers.¹⁴ Still calling its approach friendly, *Pirelli* went ahead to rally for support of major *Continental* shareholders, which was particularly necessary because - like in the *Feldmühle* case - the voting rights an individual shareholder could exercise were limited to 5 per cent.¹⁵ *Pirelli* met with fierce resistance from the *Continental* management. Although *Pirelli* managed - contravening the disclosure provisions of the Stock Corporation Act (!)¹⁶ - to pool enough shares to get rid of the 5 per

11 *Burgard*, Die Offenlegung von Beteiligungen, AG 1992, 42; *Ebenroth/Daum*, Die Kompetenzen des Vorstands einer Aktiengesellschaft, DB 1991, 1157.

12 *Frankfurter Allgemeine Zeitung*, 18 September 1990.

13 *Frankfurter Allgemeine Zeitung*, 18 September 1990.

14 *Frankfurter Allgemeine Zeitung*, 25 September 1990; *Economist*, 26 January 1991.

15 As to restrictions on voting rights see Chapter 4.3.1. at pp. 157.

16 Because of the infringement of the disclosure provision in sec. 20 of the Stock Corporation Act the Hannover Regional Court later quashed the resolution which removed the voting rights limitation from *Continental's* articles: see Landgericht Hannover, Urteil vom 29.5.1992, ZIP 1992, 1236. The decision is based on the fact that the shareholders party to the pool-arrangement were "acting in concert" and that therefore their shares had to be aggregated. This decision was affirmed by the Higher Regional Court in Celle: Oberlandesgericht Celle, Urteil vom 15.7.1992, AG 1993, 178.

cent voting right limitation, the final push for *Pirelli* came at a general meeting of *Continental* in March 1991 when the proposed merger was prevented by a blocking minority of more than 25 per cent. As in the *Feldmühle* case, it is not entirely clear which role the powerful *Deutsche Bank*, which was represented at *Continental*'s supervisory board, played in the whole affair¹⁷ and it is interesting to note that *Continental* was defended by *Morgan Grenfell*, the British merchant bank that is a subsidiary of *Deutsche Bank* since 1989.¹⁸ It is alleged that *Deutsche Bank* "convinced" the German car companies *Daimler Benz* and *Volkswagen* to buy stakes in *Continental* to mount some form of rescue operation to frustrate *Pirelli*'s efforts.¹⁹ Although finally defeated, in the opinion of many, *Pirelli* could have succeeded if they had tried more vigourously and "fortress Germany" had not been the only reason *Pirelli*'s bid failed.²⁰ A certain lack of planning as well as deep divisions among *Pirelli*'s senior managers over which course to pursue and *Mr Pirelli*'s refusal to buy shares aggressively during the course of the bid in order to come to an agreement with *Continental* probably contributed to *Pirelli*'s defeat.²¹ If *Pirelli* had succeeded in taking over *Continental*, this might have inspired other companies to bid for a German target. Yet, *Pirelli* not only failed, but also incurred huge losses believed to be in the area of DM 470 million because of share price warranties they gave to co-operating *Continental* shareholders.²² The whole affair therefore

17 Helmer, in *Frankfurter Allgemeine Zeitung*, 8. April 1993; *Economist*, 7 December 1991: Management Focus: Pre-merger management; *Economist*, 22 June 1991; *Economist*, 18 May 1991; *Economist*, 23 February 1991.

18 *Economist*, 12 September 1992: Bidding for Europe's takeover business. The article suggests that the acquisition of Morgan Grenfell by Deutsche Bank was part of a general strategy by European banks to buy British takeover expertise.

19 *Economist*, 23 February 1991 and 18 May 1991.

20 Helmer, in *Frankfurter Allgemeine Zeitung*, 8. April 1993.; *Economist*, 7 December 91: Management Focus: Pre-merger management.

21 *Economist*, 7 December 91: Management Focus: Pre-merger management. *Economist*, 30 November 1991: Europe's corporate castles begin to crack.

22 *Continental*'s share price fell by about a third during the course of the bid. As to the warranty arrangements in detail see the decision of the Regional

added to the general perception that German stock corporations are practically immune from takeover bids.²³

(3) Krupp ./ Hoesch

The third case, *Krupp GmbH's* successful merger with *Hoesch AG*, both steelmakers, was not an outright public bid either. Yet, what makes it worth mentioning here is that *Krupp's* approach to *Hoesch* was very different from the usual German business practice in that no co-operation was sought at the beginning. In October 1991 *Krupp* revealed that it had secretly acquired a 24.9 per cent stake in *Hoesch*²⁴ and hinted that its allies were holding enough shares to confer effective control on *Krupp*,²⁵ albeit due to a voting right restriction in *Hoesch's* articles *Krupp* itself - like any other shareholder - could only vote a maximum of 10 per cent of its shares in *Hoesch*.²⁶ *Krupp* then asked for a merger with its ailing rival. Although *Hoesch's* management reacted offended at first, the merger finally proceeded without a defence from *Hoesch*. Remarkably, mighty *Deutsche Bank*, which was represented on *Hoesch's* supervisory board, got wind of *Krupp's* plan only after *Krupp's* public announcement. This is very unusual indeed for such a big deal. Indicative too is the fact, that *Krupp* was not represented by one of the three traditional establishment banks - *Deutsche Bank*,

Court in Hannover: Landgericht Hannover, Urteil vom 29.5.1992, ZIP 1992, 1236; also *Burgard*, Die Offenlegung von Beteiligungen, AG 1992, 43, footnote 34b. Also *Economist*, 7 December 91: Management Focus: Pre-merger management.

23 *Economist*, 23 February 1991 and 18 May 1991.

24 Just below the 25 per cent disclosure threshold in sec. 20 AktG. However, the Securities Trading Act 1994 now requires disclosure of 5 per cent stakes. *Krupp's* way will therefore not be practicable any more. See Chapter 4.1.2.(2) at pp. 125.

25 *Economist*, 9 November 1991 and 19 October 1991.

26 *Joussen*, Die Treuepflicht des Aktionärs bei feindlichen Übernahmen, BB 1992, 1075, 1080.

Dresdner und Commerzbank - which normally handle these deals, but by the aggressive, but state-owned *WestLB*.²⁷

Especially the events surrounding *Feldmühle* and *Continental* received wide publicity and triggered much comment by academic writers²⁸ and the managements of large German stock corporations began to worry about their much enjoyed safety and independence.²⁹ Some academics believed that the repercussions of the "takeover fever" prevalent in the U.K. and the U.S. during the 1980s had finally reached Germany and expect anglo-saxon style takeovers in a not too distant future to happen in Germany. So far, however, there is very little evidence to support that view.

Apart from providing a survey of the defensive measures open to a target company (4.3.), the following chapter undertakes to outline the legal environment within which takeover bids had to take place (4.1.) and analyse in some depth the determining structural factors which are - obviously - impeding takeover bids in Germany (4.2.).

27 *Economist*, 16 May 1992: *WestLB* unbound.

28 In English: *Henle*, Defences to Corporate Takeover in Germany, [1994] 4 ICCLR 122. In German: *Burgard*, Die Offenlegung von Beteiligungen, AG 1992, 41; *Daum*, Die unkoordinierte Übernahme, S. 44 ff; *Ebenroth/Daum*, Die Kompetenzen des Vorstands einer Aktiengesellschaft, DB 1991, 1157; *Ebenroth/Rapp*, Abwehr von Unternehmensübernahmen, DWiR 1991, 1; *Knoll*, Übernahme von Kapitalgesellschaften, 1992, S. 37; *Marquardt*, WiB 1994, 537; *Salje*, Feindliche Übernahmen, JA 1990, 321; *Sandberger*, Teilübernahmeangebote und Zwangsübernahmeangebote im Europäischen Takeover-Recht, DZWIR 1993, 319.

29 See for instance *Economist*, 26 December 1992: Rattling the Vorstand: Corporate governance in Germany. *Die Zeit*, 16 August 1991; *Burgard*, Die Offenlegung von Beteiligungen, AG 1992, 41, footnote 3; *Joussen*, Die Treuepflicht des Aktionärs bei feindlichen Übernahmen, BB 1992, 1075. Also *Werner*, Probleme feindlicher Übernahmeangebote, p. 7.

4.1. The Regulatory Framework

Given the rareness of public takeover bids in Germany, it is not surprising that there are no legally binding rules specifically designed to govern public takeover bids. There are, however, a few disclosure provisions to be noted in the Stock Corporations Act 1965 and the newly introduced Securities Trading Act 1994. The only rules specifically addressed to takeover bids are not legally binding. They are contained in the German Takeover Code 1995 (see APPENDIX 1).

4.1.1. The non-legal German Takeover Code 1995

A first faint debate about the regulation of takeover bids, which at that time were completely unknown in Germany, was triggered in 1974 by *Professor Pennington's "Report on Takeover and other bids"* which he prepared on behalf of the EC-Commission.³⁰ This report presented a first draft of a Takeover Directive.³¹ In January 1979, at a time when a number of other European states had already introduced some form of takeover regulation, the German deliberations finally resulted in the non-binding Takeover Recommendations 1979.³² They were drafted by the so-called Stock

30 EC Doc. XI/56/74-E. As to the Pennington Report see *Bradley*, Harmonising Takeover and Merger Regulations within the EEC, *Company Lawyer*, Vol. 7, No. 4, p. 131, 135. See also Chapter 5.1. at p. 173.

31 See Chapter 5.1. at p. 173. For early German articles on the issue see e.g. *Behrens*, Rechtspolitische Grundsatzfragen einer Europäischen Regelung für Übernahmeangebote, *ZGR* 1975, 433; *Bess*, Eine europäische Regelung für Übernahmeangebote, *AG* 1976, 169. As to Professor Pennington's role see *Immenga/Hellberg*, Corporate Takeovers through the Public Market, p. 25.

32 For a brief analysis see *Assmann/Bozenhard*, Übernahmeangebote, p. 40. Also *Grunewald*, Was bringt der Vorschlag einer 13. EG-Richtlinie, *WM* 1989, 1235, 1236.

Exchange Experts Commission (Börsensachverständigenkommission), a private body of independent experts involved in the financial services industry appointed by the Federal Ministry of Finance which was first set up in 1968.³³ However, the Takeover Recommendations 1979 lacking any enforcement mechanism have never gained any practical relevance³⁴ and were widely criticized for being too fragmentary and vague.³⁵

Despite the absence of any real takeover bid activity in Germany,³⁶ in summer 1994 the Stock Exchange Experts Commission felt bound to deliberate on a new set of takeover rules for two reasons: First, the German debate on the takeover issue has recently been inspired by new developments on European level.³⁷ Secondly, and more importantly, it was and is widely felt that regulatory measures aimed at bringing the German stock market more in line with international standards in order to boost investor confidence in the German stock market, especially abroad, are needed. The efforts by the Stock Exchange Experts Commission can, thus, be seen as part of the wider efforts by the German government and the financial community to internationally strengthen the competitive position of Germany as a financial centre, the German slogan being the "*Finanzplatz Deutschland*" concept.³⁸ The

33 As to the institutional framework see Chapter 4.1.1.(5)(a) at p. 119.

34 Assmann, Verhaltensregeln für freiwillige öffentliche Übernahmeangebote, AG 1995, 563; Neye, Der neue Übernahmekodex, ZIP 1995, 1464; Sandberger, Teilübernahmeangebote und Zwangsübernahmeangebote, DZWIR 1993, 319, 320.

35 Assmann, Verhaltensregeln für freiwillige öffentliche Übernahmeangebote, AG 1995, 563.

36 For an empirical study see Wymeersch, Unternehmensführung in Westeuropa, AG 1995, 299, 307. Also Krause, Zur Gleichbehandlung der Aktionäre bei Übernahmeangeboten und Beteiligungserwerb WM 1996, 845; Neye, Der neue Übernahmekodex, ZIP 1995, 1464; Thoma, Der neue Übernahmekodex der Börsensachverständigenkommission, Osnabrück, Arbeitspapier 9/96, p. 4.

37 See Chapter 5.1 at pp 173 and in particular Chapter 5.1.2. at pp. 180.

38 As to these motives see, for example, Assmann, who is one of the leading German academics in this field, in Verhaltensregeln für freiwillige öffentliche Übernahmeangebote, AG 1995, 563; Baumann, who is a board member of Siemens, in Der neue Verhaltenskodex für Unternehmensübernahmen, WM 1996, 901, 902; Breuer, who is a board member of the Deutsche Bank, in Handelsblatt, 23 June 1994; Neye, who

German Takeover Code was adopted in July 1995 and entered into "force"³⁹ in October 1995 (see APPENDIX 1). As *Hans-Werner Neye*, who took part in the discussions leading to the adoption of the new rules,⁴⁰ reports, the deliberations on the new Takeover Code were heavily influenced by the concept and ideas of the City Code and the (previous) 1989/1991 proposal for a European Takeover Directive, which itself was also modelled on the City Code.⁴¹ It therefore not surprising that the German Takeover Code shows many features of the City Code.

(1) Legal nature

The Stock Exchange Experts Commission which adopted the German Takeover Code is a private body of independent experts with backgrounds in industry and the investment services sector including an official from the German Ministry of Finance. Hence, the rules drawn up by this body can - as the English City Code - only be voluntary in nature and do not have the force of law.⁴² Unlike the City Code, however, which claims in its introduction to represent "*the collective opinion of those professionally involved in the field of takeovers as to good business standards and as to how fairness to shareholders can be achieved*"⁴³ no similar statement can be found

is a high-ranking official at the German Ministry of Justice and took part in the discussions leading to the adoption of the new Takeover Code, in *Der neue Übernahmekodex*, ZIP 1995, 1464, 1465; *Schuster*, Head of the Fundamental Issues Group at Deutsch Morgan Grenfell, in *Neue Regeln für Übernahmen*, *Die Bank* 1995, 609; *Thoma*, *Der neue Übernahmekodex der Börsensachverständigenkommission*, Osnabrück, Arbeitspapier 9/96, S. 4.

39 It remains to be seen whether "force" is the correct word in this context. See Chapter 4.1.1.(5)(b) at p. 120.

40 *Neye*, *Der neue Übernahmekodex*, ZIP 1995, 1464, 1465.

41 See Chapter 5.1. at pp. 173.

42 See German Takeover Code, Introduction: "*The Takeover Code is a set of recommended rules of conduct for parties involved in voluntary public takeover offers....*"

43 City Code, Introduction, para 1(a).

in the German Code. There hardly could be, critics of the German Takeover Code might add, as no public discussions or consultations took place prior to the adoption of the German Code by the Stock Exchange Experts Commission.⁴⁴ It is therefore questionable whether the German Code reflects the collective opinion of those involved in (maybe future) takeover bids rather than just the opinion of the Stock Exchange Experts Commission. Not surprisingly, the German Code has been criticized by practitioners and academics alike,⁴⁵ in particular with respect to the newly introduced mandatory bid rule.⁴⁶ Although the new German Takeover Code has clearly sparked a lively debate as the number of recent articles cited in the footnotes clearly indicates, given that it has been “*in force*” for a relatively short period of time only, it is too early to draw any definite conclusions as to its acceptance in practice.⁴⁷

(2) Scope and Structure

The German Takeover Code containing 24 rather short articles is divided into the following seven sections:

Introduction

Definitions

General Principles

Conduct of the Offer

Duties of the Offeror

Duties of the Target

44 This has been criticized by *Kallmeyer*, *Der Übernahmekodex der Börsensachverständigenkommission*, AG 1996, 169. As to the members of the Stock Exchange Experts Commission see Chapter 4, footnote 80.

45 See in particular *Kallmeyer*, *Der Übernahmekodex der Börsensachverständigenkommission*, AG 1996, 169; also *Assmann*, *Verhaltensregeln für freiwillige öffentliche Übernahmeangebote*, AG 1995, 563, 570; *Friese*, *Verraten und verkauft*, Capital 11/1995, p. 113; *Klemm*, *Der Übernahmekodex ist zu vage*, *Börsenzeitung* Nr. 85 of 3 May 1996.

46 Art. 16 of the German Takeover Code. See Chapter 4.1.1.(4) at pp. 116.

47 For details see Chapter 4.1.1.(5)(b) at pp. 120.

Takeover Commission

It applies to public offers for stock corporations (Aktiengesellschaften) or partnerships limited by shares (Kommanditgesellschaften auf Aktien) which have its corporate seat in Germany and are listed on a German Stock Exchange or traded in the over-the-counter market (Freiverkehr).⁴⁸ The scope of the City Code is wider as it applies to offers for both listed and unlisted public companies.⁴⁹ Bids for non-German targets listed on a German Stock Exchange are, hence, not governed by the new Code.

In terms of securities, the German Code covers primarily offers for securities which directly or indirectly confer voting rights, but provides that it is to be applied to offers for non-voting preference shares analogously.⁵⁰ In this last respect the German Code is wider than the City Code which does not apply to non-voting preference shares.⁵¹ The legal nature or origin of the bidder is as under the City Code irrelevant.⁵²

From a German point of view it is conspicuous that the Takeover Code is, untypical for German regulations, preceded by an introduction and a section of definitions which betrays the English model. Although the whole text of the German Takeover Code comprises only a couple of pages, as APPENDIX 1 shows, and is therefore far less detailed than the City Code which is a book containing more than 100 pages,⁵³ the basic regulatory approach is the same. In harmony with the City Code, the Takeover Code gives prominence to a number of *General Principles*⁵⁴ and stipulates in words almost identical to those of the City Code that the rules "*must be observed not only according to its letter but also according to its*

48 German Takeover Code, Definitions "Target".

49 See Chapter 3.1.1.(1) at pp. 30.

50 German Takeover Code, Definitions "Securities".

51 See Chapter 3.1.1.(1) at pp. 30.

52 German Takeover Code, Definitions "Offeror".

53 As to the structure of the City Code see Chapter 3.1.1.(1) at p. 30.

54 Articles 1-6 of the German Code. See Chapter 4.1.1.(3) at pp. 112.

underlying purpose."⁵⁵ As under the City Code, the German Takeover Code empowers the German Takeover Commission, a body comparable to the English Panel on Takeovers and Mergers,⁵⁶ to modify or waive the application of individual provisions if their application would damage legitimate interests of the offeror, the target, or shareholders.⁵⁷ Hence, both sets of rules aim for a code which is flexible and, unlike legal statutes, easy to amend.

(3) Fundamental Principles underlying the Takeover Code

As the German Takeover Code is modelled on the English City Code, it not surprising that it is governed by the same basic regulatory principles, most notably the principles of equality and adequate shareholder information. Some of these principles are contained in the section entitled "*General Principles*", others are to be found in the remaining sections of the German Code.

(a) Equality of Treatment

Article 1 of the German Takeover Code, which could well be a direct translation of General Principle 1 of the City Code, provides that all shareholders of the target company are to be treated equally

55 German Takeover Code, Introduction. The City Code provides in its Introduction, para 3(b), that the Rules and General Principles "*are to be interpreted to achieve their underlying purpose. Therefore, their spirit must be observed as well as their letter and the Panel may modify or relax the application of a Rule if it considers that, in the particular circumstances of the case, it would operate unduly harshly or in an unnecessarily restrictive or burdensome or otherwise inappropriate, manner.*"

56 As to further details see Chapter 4.1.1.(5)(a) at pp. 119.

57 Article 23 of the German Takeover Code.

by an offeror. This very basic tenet is further specified by various other articles.

The principle of equality is of relevance, for example, in connection with partial offers in respect of which the Takeover Code⁵⁸ provides in harmony with the City Code⁵⁹ that oversubscribed offers are to be scaled down proportionally. As partial offers are, contrary to the City Code, not subject to the consent of the Takeover Commission or any additional qualification, this provision could well become of particular importance if public bids were to become popular in Germany.

As under the City Code, equality of treatment is also required in respect of the terms of the offer.⁶⁰ Article 13 provides that if the offeror acquires during the offer period⁶¹ shares on terms more favourable than specified in the offer document, these more favourable terms must be made available to all target shareholders. Article 14 stipulates that if the offeror makes a better second offer during the offer period, those shareholders who already have accepted the first offer must be made available the terms of the improved second offer. Contrary to Rule 35.1 of the City Code, which prohibits new offers by the offeror for the same target for a period of 12 months following the closing of the previous bid, there is no such restriction under the German Takeover Code. However, Article 15 provides that if the bidder comes up with an improved offer within a specified period⁶² of time of not less than 12 months after the previous bid, the more favourable terms must be made available to those who have already accepted the first bid. Furthermore, the principle of equality is of relevance in connection with the terms of

58 Article 10 of the German Takeover Code.

59 Rule 36.7 of the City Code.

60 See Chapter 3.1.1.(2)(a) at pp. 32.

61 Article 11 of the German Code requires a minimum offer period of 28 days. Under Rule 31.1 of the City Code the minimum offer period is 21 days. Both Codes limit the maximum offer period to 60 days.

62 To be specified in the offer document.

the mandatory offer required under Article 16. This last issue will be discussed in more detail at a later stage.⁶³

(b) Adequate Information

In line with General Principle 4 of the City Code,⁶⁴ Article 2 (1) of the German Takeover Code undertakes to ensure that all shareholders of the target company are given sufficient time and information to reach a properly informed decision on the offer. Most important in terms of information is the offer document the content requirements of which are less stringent than those of the City Code as a comparison between Rule 24 of the City Code and Article 7 of the Takeover Code shows. Unlike the City Code there is no provision which requires the offeree board to obtain competent independent advice which is to be made known to the shareholders. However, according to Article 18 of the German Takeover Code, the offeree board has to publish without delay "*a reasoned statement of its position in relation to the offer.*"

Under Rule 20.2 of the City Code any information given by the target company to one offeror or potential offeror must be given equally and promptly to any (potentially) competing bidder, even if that bidder is less welcome. Albeit Article 2 (2) basically provides for the same right, this right is somewhat more restricted under the German Takeover Code as the management board of the target is obliged to make such information available to a (potential) competing bidder only "*upon proper exercise of its discretion and in the interests of the holders of securities*" and where that bidder has "*demonstrated a genuine interest in taking over the target.*" Hence, the situation of (potential) competing bidders is somewhat less

63 See Chapter 4.1.1.(4) at pp. 116.

64 See Chapter 3.1.1.(2)(b) at pp. 33.

favourable than in Britain, the standard of equality is lower. This rule appears to reflect to some extent the different German takeover-culture which has traditionally been sceptical about the idea of an auction between competing bidders. Another provision which seems to mirror the less confrontational takeover culture in Germany is Article 4 of the German Code which provides that "*the announcement of an offer should generally be preceded by consultations between the offeror and the target.*" There is no provision to this effect in the City Code. Moreover, unlike the City Code, Article 5 of the German Takeover Code stipulates that prior to making a public bid the offeror is obliged to inform the target, the relevant German Stock Exchanges, the Federal Supervisory Office for Securities Trading and the Executive of the German Takeover Commission.⁶⁵

(c) Transparency in dealings

Dealings prior to the announcement of the intention to make an offer are governed solely by the insider trading provisions of the German Securities Trading Act.⁶⁶ During the offer period,⁶⁷ dealings in relevant securities are to be disclosed to the Takeover Executive the following business day.⁶⁸ As a matter of course, both the British and the German rule book prohibit the creation of a false market by

65 Article 5 of the German Takeover Code.

66 Sec. 12-20 of the German Securities Trading Act. The City Code contains in Rule 4.1 some specific provisions regarding the period prior to an offer.

67 As to the lengths of the offer period see Chapter 4.1.1.(3)(a) footnote 61.

68 Article 12 of the German Takeover Code, which is broadly in line with Rule 8.1 (Notes 3, 4 and 5) of the City Code. See also Chapter 3.1.1.(2)(c) at pp. 34.

those involved in the bid.⁶⁹ Any announcement must be prepared with the highest standard of care and accuracy.⁷⁰

(d) Restrictions on frustrating action

Regarding defensive measures, Article 19 of the Takeover Code is largely in line with Rule 21 of the City Code⁷¹ which prohibits the frustration of a bona fide offer during the offer period. The defences open to a German target will be examined in further detail in Chapter 4.4.⁷²

(4) Mandatory Offer

The most salient and most controversial feature of the new German Takeover Code is the mandatory offer requirement provided for in Articles 16 and 17.⁷³ A comparison with the mandatory bid requirement contained in Rule 9 of the City Code shows, however, that the respective provisions differ in virtually all important aspects, including, *inter alia*, the thresholds, the timetable, and the determination of the offer price.

Notwithstanding various exceptions pursuant to which a mandatory offer is dispensable, a mandatory offer has in principle to be made once the acquirer including persons acting in concert⁷⁴

69 Article 3 of the German Takeover Code = General Principle 6 of the City Code.

70 Article 8 of the German Takeover Code; General Principle 5 of the City Code.

71 See Chapter 3.1.1.(2)(d) at pp. 35 and Chapter 3.4. at pp. 85.

72 See Chapter 4.4. at pp. 165.

73 For a critical discussion see *Assmann*, Verhaltensregeln für freiwillige öffentliche Übernahmeangebote, AG 1995, 563, 569 et seq.

74 As to concert parties, Article 16 of the German Takeover Code refers to sec. 22 (1) of the German Securities Trading Act (APPENDIX 3).

have acquired more than 50 per cent of the voting rights in the target. The relevant threshold under the City Code is 30 per cent. Contrary to the U.K. where the mandatory bid has to be made without delay, under the German Code, the offeror has up to 21 months (!) to make the offer after passing the 50 per cent threshold for the following reason: Article 16 stipulates that a mandatory offer is dispensable if the offeror embarks following the acquisition of the majority stake on one of the reconstructions of the corporate group specified in Article 16 within a period of 18 months (see APPENDIX 1). If no such corporate reconstruction has taken place during that period, the offeror then has a further 3 months within which he has to make the mandatory offer. In the meantime the minority shareholders left in the target are kept in suspense. This rule is to some extent a result of the different concept of minority shareholder protection through the law of groups in Germany.⁷⁵ However, this rule might well cause speculation, uncertainty, and maybe insider dealing in the market of the target shares during the long waiting period. It is also open to question whether that rule can be considered fair to investors who are after all left in a limbo. Whether this rule is able to enhance investor confidence in the German Stock Exchange market both nationally and internationally appears, thus, somewhat doubtful.⁷⁶

According to Article 16, a mandatory offer is also dispensable where the acquirer purchased the relevant shares in order to place them with a third party, where the threshold was passed unintentionally and subsequently reduced, or where the acquirer is released by the remaining shareholders of the target company from the obligation to make an offer. Furthermore, Article 23 stipulates that the Takeover Commission may release an acquirer from the obligation to make a full offer if "*legitimate interests*" would be

75 See Chapter 4.2.5. at pp. 151.

76 Critical also Thoma, Der neue Übernahmekodex der Börsensachverständigenkommission, Osnabrück, Arbeitspapier 9/96, p. 11, 15.

damaged otherwise. A definition or examples illustrating this somewhat vague term are not provided.

If despite the numerous exceptions it ever comes to a mandatory bid under Article 16 of the voluntary German Takeover Code,⁷⁷ the pricing rules of Article 17 are to be regarded. Contrary to the City Code, which requires the offer to be made at not less than the highest price paid for target shares during the offer period or in the preceding 12 months, the German rules are far less stringent.⁷⁸ Article 17 of the German Code differentiates between the situation where the acquirer has following the passing of the 50 per cent threshold made no further purchases and where he has made further purchases. In the first case, paragraph 1 of Article 17 stipulates that the offer price "*must reasonably reflect the then current market price. It should not be more than 25 per cent below the price which the majority shareholder paid for securities of the target in the six months period prior to the passing of the threshold.*" If the acquirer has made further purchases, paragraph 2 of the mentioned article provides that after passing the 50 per cent threshold, the acquirer then has to offer "*the weighted average price paid in the course of such purchases*" provided it is higher than the price to be offered under paragraph 1. Hence, regarding the pricing of the mandatory offer, the provisions of the German Takeover Code provide for a rather limited degree of equal treatment of target shareholders that falls clearly short of the strict standards prescribed by the City Code.

(5) Administration and Enforcement

Although the institutional structure set up by the German Takeover Code is clearly modelled on the British Panel on

77 Sceptical as to the future practical relevance of the mandatory bid provision also Neye, *Der neue Übernahmekodex*, ZIP 1995, 1464, 1466.

78 Rule 9.5 of the City Code.

Takeovers and Mergers, the differences regarding the enforcement of the German rules are substantial.

(a) Institutional Framework

Three different bodies are involved in the administration of the German Takeover Code all of which are private in nature:

- (1) the Stock Exchange Experts Commission
- (2) the Takeover Commission
- (3) the Executive⁷⁹

The Stock Exchange Experts Commission has drawn up the Takeover Code. The Ministry of Finance appoints and dismisses the members of the Stock Exchange Experts Commission, but there is no legal basis for this and the government has no control or influence over the independent experts.⁸⁰ Apart from amending the Takeover Code and the drafting of internal procedural rules, the main responsibility of the experts is to appoint the members of the Takeover Commission, its chairman and deputies.

79 Address: Übernahmekommission, Geschäftsstelle, c/o Deutsche Börse AG, Börsenplatz 7-11, 60313 Frankfurt a.M., Tel. 0049/69/21018276, Fax 0049/69/21011331.

80 As at June 1996 the members were: *Dr. K.-H. Baumann* (board member of Siemens AG); *Dr. D. Breipohl* (board member of Allianz AG); *Dr. R.-E. Breuer* (board member of Deutsche Bank AG); *Prof. Dr. H. E. Büschgen* (University of Cologne); *G. Eberstadt* (board member of Dresdner Bank AG); *U. E. Flach* (board member of DG Bank); *J. W. Gaddum* (vice-president of the Deutsche Bundesbank); *M. Hagen* (ministry for economics of Lower Saxony); *D. Kauffmann* (representative of a small-investor protection association = Schutzgemeinschaft der Kleinaktionäre); *Dr. A. Kollar* (board member of Westdeutsche Landesbank); *H. Loehr* (board member of Bayer AG); *H. P. Schreib* (representative of an investor protection association = Deutsche Schutzvereinigung für Wertpapierbesitz); *Dr. W. Seifert* (board member Deutsch Börse AG); *L. Tröbinger* (board member of Bankgesellschaft Berlin AG); *Dr. J. Henke* (German Ministry of Finance); *K.-B. Caspari* (German Ministry of Finance); *G. Wittich* (Supervisory Office for Securities Trading); *H.-J. Schwarze* (Secretary of the Stock Exchange Experts Commission).

The Takeover Commission, consisting of 7 to 15 members with backgrounds predominantly in the financial services industry,⁸¹ is comparable to the British Takeover Panel. The members are appointed for a period of five years reappointment being possible. The Takeover Commission appoints the Head of the Executive,⁸² decides on requests by the parties to release them from certain provisions of the Takeover Code,⁸³ and hears appeals from decisions by the Executive.⁸⁴

The Executive carries on the day-to-day work. It examines whether offer document complies with the provisions of the German Code and may publish comments, recommendations and decisions in relation to cases.⁸⁵

(b) Enforcement Mechanism?

Contrary to the complex enforcement-network examined in relation with the City Code,⁸⁶ in terms of enforcement there is little one can say with respect to the German Takeover Code. Article 21 of the German Code asks potential offerors, targets and providers of investment services to "*acknowledge the provisions of this Code.*" A

81 Article 20 (1)-(4) of the German Takeover Code. Members of the Takeover Commission as at June 1996: *H. Loehr* (board member Bayer AG); *Dr. R. E. Breuer* (board member Deutsche Bank AG); *J. Benner-Heinacher* (representative of a small-investor protection association = Schutzgemeinschaft der Kleinaktionäre); *Dr. D. Breipohl* (board member Allianz Holding AG); *G. Eberstadt* (board member Dresdner Bank AG); *Dr. M. Gentz* (board member Daimler Benz AG); *Prof. Dr. Dr. H. Havermann* (KPMG); *Prof. Dr. Dr. K. Hopt* (Hamburt University); *Dr. N. Juchem* (Bayrische Vereinsbank AG); *D. Kauffmann* (representative of an investor protection association = Deutsche Schutzvereinigung für Wertpapierbesitz); *Dr. A. Kollar* (board member Westdeutsche Landesbank); *Dr. K. J. Lauk* (board member VEBA AG); *M. Mathes* (Union-Investment Gesellschaft mbH); *Dr. W. G. Seifert* (board member Deutsche Börse AG).

82 Article 20 (7) of the German Takeover Code.

83 Article 23 of the German Takeover Code.

84 Article 21 (2) of the German Takeover Code.

85 Article 21 (2) of the German Takeover Code.

86 See Chapter 3.1.2.(3) at pp. 44.

list featuring those who have acknowledged the German Code is to be published by the Executive. As of end of April 1996, of 674 listed German companies 229 "acknowledged" the Code.⁸⁷ However, according to a report in a leading German business magazin in August 1996 the 100 biggest listed stock corporation in Germany 47 have so far refused to acknowledge which may well be considered as a serious blow for the new regulatory system.⁸⁸ Among the top 100 companies which have refused acknowlegdement so far a numerous well respected blue-chip corporations such as the carmakers BMW and VW.

If the Executive has found a party, which has acknowledged the German Code, to have acted in contravention of it, it may publish after having granted that party a hearing an adverse comment.⁸⁹ No further sanctions are available, neither to the Executive nor to the Takeover Commission or the Stock Exchange Experts Commission!

Time will tell whether companies feel bound by their non-contracual good-will acknowledgement in any "hard cases" in future. Given that self-regulation has in the past never really been taken seriously in Germany,⁹⁰ it seems rather unlikely that a purely "social" acknowledgement of the Code will be enough to command compliance with the new Code when it counts.

87 Thoma, Der neue Übernahmekodex der Börsensachverständigenkommission, Osnabrück, Arbeitspapier 9/96, p. 25.

88 *Wirtschaftswoche*, Nr. 34 of 15.8.1996, p. 68-69.

89 Article 21 (2) of the German Takeover Code.

90 A very eloquent example are the past experiences with the voluntary insider-rules. See in detail *Mennicke*, Insider regulation in Germany: the change from self-regualation to criminal law, *Company Lawyer*, Vol. 15, No. 5, p. 155 et seq. (1994).

(6) Summary

Although the German Code shares the basic values of the City Code (equality, adequate information, transparency, no frustrating action), it deviates in detail on many crucial aspects, in particular in relation to the mandatory offer requirement. The most notable difference, however, is the almost complete lack of any (hard) enforcement mechanism. Albeit the German Takeover Code might be considered a first cautious step into the right direction and might have some beneficial public-relations effects in terms of increasing investor confidence in the *Finanzplatz Deutschland*, as long as there is no effective enforcement mechanism in place, it appears too early to take the German Code seriously as a regulatory framework. It clearly is not in the same class with the City Code and given the different German tradition, business culture and constitutional background, it seems rather unlikely that it ever will be.

4.1.2. Disclosure Provisions

The merits of disclosure provisions have always been controversial in Germany. When disclosure provisions were first introduced into the law of stock corporations through the Stock Corporations Act 1965 many considered them a contravention of a claimed “*principle of anonymity*”.⁹¹ Due to the predominant use of bearer shares investors otherwise enjoyed complete privacy and not even the company itself knew who its owners were. As a result of the controversy, the provisions introduced in the Stock Corporations Act 1965 clearly bear the marks of compromise. However, the newly introduced Securities Trading Act 1994 has brought about quite

91 See *Emmerich/Sonnenschein*, Konzernrecht, § 6 II 1 with further references.

dramatic changes and put - as far as its scope reaches - a sudden end to the so much cherished culture of secrecy. The following chapter undertakes to analyse the existing disclosure provisions highlighting the effect the recent changes may have in terms of public takeover bids.

(1) The Stock Corporations Act 1965

As far as stock corporations are concerned, Section 20 of the Stock Corporations Act is the cornerstone of the German disclosure provisions (see APPENDIX 2).⁹² It has been in force since 1965 and applies to all stock corporations. Under section 20 only two disclosure thresholds exist. An enterprise holding shares in a stock corporation must inform the respective stock corporation for the first time when its holding exceeds 25 per cent and for the second time when it exceeds 50 per cent. It must also be disclosed if the holding falls below the mentioned thresholds. There is, however, no obligation to state the precise size of the holding. It is sufficient to announce that, for example, the 25 per cent threshold has been exceeded, which can mean anything between 25 and 49 per cent. Furthermore, it should be noted that section 20 of the Stock Corporations Act applies only to enterprises.⁹³ Private investors are regardless of the size of their stake not covered by section 20.

Compared to British standards set by the Companies Act 1985, the German disclosure provisions in the Stock Corporations Act 1965 seem remarkably lax.⁹⁴ The British Companies Act 1985 requires

92 *Burgard*, Die Offenlegung von Beteiligungen, AG 1992, 41; *Emmerich/Sonnenschein*, Konzernrecht, § 6 I-IV.

93 This means any form of corporation, including partnerships. See *Hüffer*, Aktiengesetz-Kommentar, § 15 Rn. 6 and § 20 Rn. 2.

94 For a very critical discussion of the German disclosure provisions in particular see *Adams*, Die Usurpation von Aktionärsbefugnissen mittels Ringverflechtung in der "Deutschland AG", AG 1994, 148, 153 et seq.

disclosure of the precise size of the stake once a person has acquired an interest in 3 per cent or more of the voting rights in a public company and thereafter if there is any increase or decrease.⁹⁵ Hence, the British provisions effectively prevent a bidder from secretly building up a stake sufficiently large to launch a bid taking both the target and the market by surprise.

Apart from the very high thresholds, what makes the situation in Germany worse is that the few provisions contained in the Stock Corporations Act have never been properly enforced which is unanimously admitted in Germany.⁹⁶ According to subsection 7 of section 20 the only consequence of an infringement of the disclosure obligation is that the shareholder's membership rights may not be exercised until he discloses properly. This means in practice that he must not vote his shares nor does he receive any dividend and neither can he exercise any pre-emption rights. If in such a situation the shareholder votes his shares anonymously nevertheless, he is liable to a rather low maximum fine of DM 50.000 and resolutions passed because of these votes in a general meeting are liable to be rescinded, as was the case in *Pirelli's* takeover attempt. This, of course, presupposes that he is caught. Once a previously defecting shareholder has disclosed his interest properly, all his membership rights revive. One school of thought interpretes section 20 even in the way that after the proper disclosure the shareholder is retroactively entitled to the full dividend!⁹⁷ Regardless of one's opinion concerning this last point, there can be no doubt that the legal consequences of a contravention of the disclosure provisions can not seriously deter a potential bidder from breach of the disclosure provisions. Besides, with banks acting as proxies and the common use of bearer shares, the veiling of the true ownership of

95 See section 199 (2) CA 1985. For an analysis Gower, *Principles of Modern Company Law*, pp. 613.

96 *Emmerich/Sonnenschein*, *Konzernrecht*, § 6 II 1; V.

97 See *Hüffer*, *Aktiengesetz-Kommentar* § 20 Rn. 8 with further references.

shares is rather facilitated by the legal environment and the chances to actually get caught seem rather dim.

Coming back to the takeover question, these rather lenient disclosure provisions may well have been one of the reasons why public bids have in the past not been seen as a practical, or necessary, means to win control. In a legal environment which treasures secrecy and does not require the purchaser to treat the target's shareholders equally by way of a mandatory offer or the requirement to pay a premium for corporate control, there seems to be no real need for a public bid. Effective control may - at least in most cases - cheaper be acquired by secretly purchasing *de facto* control on the Stock Exchanges and buying from major single shareholders outside the Stock Exchanges, which, of course, is standard practice in Germany.⁹⁸ The point here made is quite well demonstrated by the *Flick* case. When the *Flick* brothers announced publicly that they intended to win control in *Feldmühle*, share-prices skyrocketed which caused them to withdraw. When they went on to acquire by stealth what ultimately amounted to a 40 per cent stake, they made a huge profit. Acquiring a 24.9 per cent stake secretly was also crucial in the reported *Krupp/Hoesch* case. However, due to the newly introduced Securities Trading Act 1994 the situation has changed.

(2) The Securities Trading Act 1994

"German boardrooms blink in clear light of disclosure" proclaimed the Times in 1995.⁹⁹ As far as listed stock corporations are concerned, this is true. For non-listed stock corporations,

98 *Daum*, Die unkoordinierte Übernahme einer Aktiengesellschaft, p. 70-74;
 Peltzer, Hostile Takeovers in der Bundesrepublik, ZIP 1989, 69 at 72;
 Financial Times, 18 December 1992: German takeover rules criticised;
99 *Times*, 16 January 1995.

however, the described insufficient disclosure regime of the Stock Corporations Act 1965 remains relevant.

It might well be argued that the recent changes in German investment law, of which the Securities Trading Act 1994 is only the most important part, mark the beginning of a new era for the German securities markets.¹⁰⁰ The scope of the Securities Trading Act goes beyond the introduction of new disclosure provisions for listed stock corporations.¹⁰¹ It implements the Insider-Dealing-Directive¹⁰² and makes insider-dealing, which seemed to be a rather popular boardroom sport, enjoyed even by the former chairman of the most powerful trade union in Germany,¹⁰³ for the first time ever illegal. The new act also contains legally binding rules of conduct for investment firms and securities dealers, thus, implementing Art 10 and 11 of the Directive on Investment Services in the Securities

100 Weber, *Deutsches Kapitalmarktrecht im Umbruch*, NJW 1994, 2849.

101 For a thorough and detailed commentary on the new Securities Trading Act see *Assmann/Schneider*, *Wertpapierhandelsgesetz*, Köln 1995. The Securities Trading Act establishes for the first time a supervisory authority, the Federal Authority for the Supervision of Trading in Securities (Bundesaufsichtsamt für den Wertpapierhandel), charged with monitoring the securities markets, thus exercising functions roughly comparable to the London Stock Exchange and the SIB. Furthermore, the Act finally implements the Insider-Directive (89/592 [1989] O.J. L334/30) and renders insider transactions for the first time in German law illegal. It also introduces legally binding rules of conduct for investment firms and securities dealers, thus implementing prematurely Art 10 and 11 of the Directive on Investment Services in the Securities Field (93/22 [1993] O.J. L141/27). See Weber, *Deutsches Kapitalmarktrecht im Umbruch*, NJW 1994, 2849. As to the new insider regulations see *Mennicke*, *Insider regulation in Germany: the change from self-regulation to criminal law*, *Company Lawyer*, Vol. 15, No. 5, p. 155 (1994).

102 89/592 [1989] O.J. L334/30

103 *Franz Steinkühler*, being the chairman of the Metal Workers Union (IG Metall) and a member of the *Daimler Benz AG* supervisory board as an employee representative, was caught red-handed in Summer 1993 when he bought shares in *MAH* worth DM 1.000.000 prior to an acquisition of that company by *Daimler Benz* of which he because of his position confidentially knew. He made a profit of DM 100.000 in a few days, which by any standards, especially by working class standards is remarkable. However, after a some days of denying, he resigned. The only really remarkable thing about this affair is that *Steinkühler* got caught at all, the reason being a highly unusual coincidence, namely that a bank employee privy to *Steinkühler's* private transactions acted in gross breach of his duty of secrecy and made *Steinkühler's* share-dealings public. To the *Steinkühler* case see also *Mennicke*, *Insider regulation in Germany: the change from self-regulation to criminal law*, *Company Lawyer*, Vol. 15, No. 5, p. 155 (1994).

Field.¹⁰⁴ To monitor and enforce the new disclosure, insider-dealing, and conduct rules, a new public agency was created: the Federal Authority for the Supervision of Trading in Securities (Bundesaufsichtsamt für den Wertpapierhandel), located in Frankfurt am Main. Although most of the new legislation is based on European directives, it fits well into the German government's ambitious "*Finanzplatz Deutschland*" concept which is designed to lift the German securities industry to the international standards and attract more foreign investors.¹⁰⁵ In the context of public takeover bids the disclosure provisions are most important and the following paragraph will focus on them.

The new disclosure provisions basically implement - with a four-year delay¹⁰⁶ - the provisions of the Major Shareholdings Directive.¹⁰⁷ Section 21 of the Securities Trading Act now requires disclosure of a holding when 5, 10, 25, 50 or 75 per cent are exceeded or when a stake falls below any of these marks (see APPENDIX 3). An indication that the German government is serious about its "*Finanzplatz Deutschland*" concept is that the lowest threshold of 5 per cent is below the Directive's minimum requirement of 10 per cent.¹⁰⁸ The acquirer has to notify the target company and the newly established Bundesaufsichtsamt within 7 days from the day of the transaction.¹⁰⁹ The target company has to publish these notifications within 9 days in the official Securities-Gazette.¹¹⁰ Contrary to the Stock Corporations Act, the exact size of the stake has to be revealed and the disclosure requirement is not restricted to

104 93/22 [1993] O.J. L141/27. This directive had to be implemented by 1 January 1996.

105 As to these motives in the context of the new German Takeover Code 1995 see Chapter 4.1.1. at pp. 107.

106 The directive was due to be implemented by January 1, 1991. Section 21 of the Securities Trading Act is came into force at January 1, 1995.

107 88/627 [1988] O.J. L348/62. As to the implementation in Britain see *Palmer's Company Law*, para 16.115 et seq.

108 In Britain under sec. 199 (2) CA 1985 a 3 per cent interest has to be closed.

109 Sec. 202 of the British CA 1985 allows only a 2 day period.

110 Wertpapiermitteilungen. Sec. 25 of the Securities Trading Act.

enterprises. Section 22 of the Securities Trading Act defines in some detail under which circumstances shares held by a third person or company are to be aggregated to the acquirer's shares. Contravention of the disclosure provisions in the Securities Trading Act renders the transgressor liable to a fine. Contrary to the Stock Corporations Act this liability arises automatically when the acquirer does not comply with the disclosure provisions, and it does not depend on him voting the shares. However, bearing in mind the large sums involved in takeover transactions, it seems questionable whether the maximum fines involved - a maximum of DM 500.000 for the defective acquirer - really constitutes a serious deterrent. Furthermore, as highlighted before the use of bearer shares and the role of the banks as proxies make it difficult to unveil the true ownership of shares. It remains to be seen, thus, how the new rules will work in practice and to what extent the new Bundesaufsichtamt für Wertpapierhandel is able to enforce them.

However, as far as the "market for corporate control" is concerned, it appears likely that - compliance with the new rules assumed - the common German practice to acquire large stakes or even control by stealth will change. Acquisitions of major stakes on the Stock Exchange will not go unnoticed any more and, thus, cause the target's share price to rise, making the acquisition more costly. With the new disclosure provisions in force for a relatively short period of time only,¹¹¹ it remains to be seen which the effect in terms of takeover activity will be. Because of the early disclosure now required, the target management will be aware of a potential takeover very early on. This, in turn, will afford them considerably more time to install defensive measures and it will not be possible any more for a predator to outwit the target management by the sort of surprise-attack seen in the *Krupp/Hoesch* case.¹¹² Looked at it that way and bearing in mind that German managers are at least not

111 January 1, 1995.

112 See Chapter 4(3) at pp. 105.

to the same extent as their British colleagues restricted from taking defensive actions,¹¹³ the new disclosure provisions may have the effect of making non-agreed takeovers - inadvertently - even more difficult.

The new provisions may also change the way in which corporate control is normally transferred in Germany. With major acquisitions through the stock exchanges now being less attractive, it might turn out that predators in future increasingly consider public takeover bids as means to win corporate control over a stock corporation in Germany. However, a more likely scenario seems to be that dawn raids become more popular in order to avoid the negative price effects of early disclosure - a development seen in Britain decades ago and now regulated against by the Rules Governing Substantial Acquisitions,¹¹⁴ but not restricted in Germany.

4.1.3. Developing a regulatory framework?

In the absence of a legally binding takeover code, efforts have been made to develop a regulatory framework by having recourse to general concepts of German civil law.¹¹⁵ Law in Germany, as a civil law country, is primarily based on precise statutes. However, where statutes do not exist, where they are insufficient or flawed, it is traditionally left to academics, mainly the law professors, and the courts to fill the gaps. The legal community discusses and elaborates different dogmatic concepts and forms after some time a leading opinion, the so-called "*herrschende Meinung*", which carries in practice quite some authority and is after a period of time often adopted by the courts. Many fields of law, like the law of tort or

113 As to the academic controversy see Chapter 4.4. at pp. 165.

114 See Chapter 3.1.3. at pp. 56.

115 See especially *Assmann/Bozenhard*, *Übernahmeangebot*, p. 55-106; also *Daum*, *Die unkoordinierte Übernahme einer Aktiengesellschaft*, p. 59 et seq.

labour law, are to a large extent governed by this kind of case law. The law of takeovers could, in the absence of a takeover code, in the opinion of some academics become a further example.

It is acknowledged that the duties imposed by the law of tort are not sufficient to govern takeovers.¹¹⁶ It has been argued, however, that the offeror, if he already is a shareholder of the target company, is under a fiduciary duty not to harm fellow shareholders.¹¹⁷ This would according to that opinion mean that, for instance, the offeror had to disclose his interests much earlier than required by the Stock Corporations Act.¹¹⁸ The Federal Supreme Court has in the *Linotype* case acknowledged that in special circumstances a major shareholder may be under such a fiduciary duty.¹¹⁹ However, this case involved a situation where the major shareholder colluded with the company management to the detriment of the remaining shareholders. It is not yet fully established, however, in which circumstances exactly shareholders owe a fiduciary duty to the other members of the company, although further development in that area is very likely.¹²⁰ Besides, if an offeror is not a shareholder of the target company, this concept based on fiduciary duties theory runs into difficulties.¹²¹

116 *Daum*, Die unkoordinierte Übernahme einer Aktiengesellschaft, p. 54 et seq.

117 *Burgard*, Die Offenlegung von Beteiligungen bei der Aktiengesellschaft, ZIP 1992, 47 et seq. Rejecting this approach sharply: *Joussen*, Die Treuepflicht des Aktionärs bei feindlichen Übernahmen, BB 1992, 1075 et seq. Also *Daum*, Die unkoordinierte Übernahme einer Aktiengesellschaft, p. 56.

118 *Burgard*, Die Offenlegung von Beteiligungen bei der Aktiengesellschaft, ZIP 1992, 47 et seq. Because of the new Securities Trading Act, this point is now obsolete as far as listed companies are concerned. See Chapter 4.1.2.(2) at pp 125.

119 Bundesgerichtshof "Linotype": BGHZ 103, 184, 194 = BGH WM 1988, 325.

120 *Joussen*, Die Treuepflicht des Aktionärs bei feindlichen Übernahmen, BB 1992, 1075; *Timm*, Treuepflichten im Aktienrecht, WM 1991, 481.

121 *Daum*, Die unkoordinierte Übernahme einer Aktiengesellschaft, p. 56.

It has also been suggested to apply the law of contract, which is basically contained in the Civil Code.¹²² However, the principle most relevant here is not contained in the Civil Code. It goes back to roman law and has been updated by the courts: the rule of *culpa in contrahendo*. This rule essentially imposes a duty of loyalty and fairness on prospective parties to a contract. Under this rule quasi contractual duties, which are considerably more stringent than the duties under the law of tort, exist before the parties actually enter into a contract. This rather vague concept has over the decades been put into more concrete terms by the courts. A prospective party contravening the *culpa in contrahendo* rule is in principle liable to damages.

However, in a field as complex and technical as takeovers the parties involved need clear and unmistakeable guidance. Uncertainties would undoubtedly lead to lengthy and destructive court battles, a danger well recognised in Britain.¹²³ The attempts to derive concrete takeover rules from the *culpa in contrahendo* rule may therefore be fine academically and of some use as long as a legally binding takeover code does not exist. In practice, however, only detailed and precise written rules can provide the certainty needed.

4.1.4. Summary

The legal environment concerning takeover bids in Germany is, apart from the newly introduced general disclosure provisions, largely characterised by the absence of legally binding rules. The voluntary Takeover Code 1995 can not be expected to have much bearing in practice as long as there is no effective enforcement

122 Assmann/Bozenhard, Übernahmangebote, p. 75 et seq; Grunewald, Was bringt der Vorschlag einer 13 EG-Richtlinie, WM 1989, 1233.

123 See Chapter 3.1.2.(4) at pp. 51.

mechanism in place. Because of this deficiency, equal treatment of the target's shareholders by a bidder is not guaranteed.

4.2. Structural Barriers

When it comes to barriers to non-agreed takeover bids, Germany has a notoriously bad reputation in the anglo-saxon world. *The Economist*, for instance, talks of "*fortress Germany*" and "*Germany's sometimes xenophobic industrial establishment*"¹²⁴ and claims that an "*influential old-boy network*" together with "*legal barriers*" make German stock corporations all but impregnable.¹²⁵

The following chapter tries to get to the bottom of these kind of statements by analysing in some depth the existing structural barriers. Actual defences to takeovers are considered in Chapter 4.3.¹²⁶ and Chapter 4.4.¹²⁷

4.2.1. Equity markets

It has been pointed out in Chapter 2 that the equity markets in Germany are rather underdeveloped. The economic environment is therefore somewhat obstructive to a flourishing market for corporate control. Although government initiatives - represented in Chapter 2 - endeavour to encourage the flotation of stock corporations, and probably will succeed in the long run, the number of officially listed stock corporations in Germany is still much smaller than in Britain.¹²⁸

124 *Economist*, 7 December 1991: Management Focus: Pre-merger management.

125 *Economist*, 23 February 1991: Our crowd: Corporate governance in Germany.

126 At pp. 156.

127 At pp. 165.

128 See Table 2 at p. 19.

Furthermore, the shareholder structure tends to be less open than in Britain. In non-listed stock-corporations family holdings often play the dominant role and listed companies are frequently part of a corporate group with another company holding a controlling stake,¹²⁹ the latter facilitated by the absence of a requirement of a mandatory bid. It has been estimated, thus, that the number of listed stock corporations susceptible to takeovers in terms of ownership structure hardly exceed 100, which is a small number indeed.¹³⁰

4.2.2. Two Tier Board System and Employee Representation

A bidder having acquired the majority of shares normally endeavours to replace the existing management with his confidants.¹³¹ This is, of course, all the more vital if the takeover has been hostile and the existing management can not be expected to co-operate. However, dismissing the management of a German stock corporation is not as easy a task as it is in principle in a British public company where section 303 of the Companies Act 1985 applies. The division of power in a British public company and a German stock corporation differs quite fundamentally in that in the structure of the English public company is rather straightforward with only two corporate organs - the general meeting of the shareholders and the board of directors - who share all power between them.¹³²

129 Estimates are that about 75 per cent of all stock corporations are part of a corporate group: see *Emmerich/Sonnenschein*, Konzernrecht, § 1 III 2d. For an empirical study see *Görling*, Die Verbreitung zwei- und mehrstufiger Unternehmensverbindungen, AG 1993, 538-547. Concerning cross-shareholdings as takeover barriers see Chapter 4.3.3. at pp. 164. As to the law of groups in Germany see Chapter 4.2.5. at pp. 151.

130 *Hopt*, European Takeover Regulation, p. 165, 168.

131 *Marquardt*, Gesellschafts- und steuerrechtliche Instrumente zur Abwehr feindlicher Übernahmen von Aktiengesellschaften, WiB 1994, 537, 540.

132 *Gower*, Principles of Modern Company Law, p. 147 et seq.

The German model, quite well known in Europe since its adoption by the proposed, but blocked, Fifth Directive in 1972,¹³³ is more complex. Power has to be shared between three organs: The general meeting of shareholders, the management board, and the supervisory board.¹³⁴ However, what really differentiates a German stock corporation from a British public company is the high degree of employee participation at all levels in a German stock corporation.¹³⁵

The following account examines the difficulties a bidder is likely to face at the post-acquisition stage. The removal and appointment of the members of both the management and the supervisory board in which context employee participation plays an important role are considered.

(1) The Management Board

The management board is exclusively responsible for the day-to-day management of the company.¹³⁶ The implementation of new policies by a successful bidder can therefore only be successful if the support of the management board is secured by either co-operation with or removal of the members of the incumbent management board. Neither the general meeting nor the supervisory board have the power to interfere with what is considered a managerial or executive task.¹³⁷ The law of stock corporations places great

133 First draft: [1972] O.J. C131/49. For details see *Palmer's Company Law*, para 16.402 et seq. See also Chapter 5.2. at pp. 198.

134 Management Board: Sec. 76-94 AktG. Supervisory Board: Sec. 95-116 AktG. General Meeting: Sec. 118-147 AktG.

135 A very good analysis in English provides *Hadden*, Employee Participation - What Future for the German Model?, *Company Lawyer*, Vol. 3, No. 6, p. 250 (1982). Note however the amendments made in 1994 mentioned in the text.

136 Sec. 76 AktG.

137 Sec. 76 (1), 111 (4) AktG. *Hüffer*, *Aktiengesetz-Kommentar*, § 76 Rn. 7. It is possible, however, by way of a specific provision in the articles to make certain deals or actions by the board members which are to be specified

emphasis on the independence of the management board and regards certain powers as managerial and therefore inalienable by the management board. A provision in the articles granting the general meeting the right to give directions by special resolution as Regulation 70 of Table A of the Companies Regulations 1985 in Britain does would be void under the Stock Corporations Act. The English approach is more flexible since the division of power is to a large extent left for the members to decide upon in the articles.¹³⁸ The independence of a German management board is most drastically reflected by the provisions governing their appointment and removal.

(a) Appointment of Management Board Members

The members of the management board are appointed for a period not exceeding five years by the supervisory board, and not by the general meeting.¹³⁹ Reappointment is possible, though. A new supervisory board resolution is, however, required in the latter case. Unless the articles provide for a greater majority, a simple majority of the supervisory board is needed for the appointment or reappointment. The supervisory board determines the salary of the management board members, which according to the Stock Corporations Act has to be adequate and must not be excessive.¹⁴⁰ Disproportionate severance payments would constitute a breach of duties on the part of the supervisory board. The service contracts of the board members may not exceed their term of office - a provision which effectively prevents *rolling contracts* in the form commonly

dependent upon the consent of the supervisory board, sec. 111 (4) sentence 2 AktG.

138 Pennington, Company Law, p. 572.

139 Sec. 84 (1) AktG.

140 Sec. 87 AktG.

applied in Britain.¹⁴¹ Excessive compensation packages are therefore not possible in Germany.¹⁴²

(b) Removal of Management Board Members

A member of the management board may only be removed by a resolution of the supervisory board.¹⁴³ Again, unless the articles impose more stringent rules, a simple majority suffices. Yet, even if the supervisory board decided unanimously to dismiss a member of the management board, removal is only possible if it is justified by either of the following three grounds: a gross violation of duties, incapability to manage or a vote of no confidence by the general meeting.¹⁴⁴ Hence, a predator holding the majority of shares can provide a sufficient cause to dismiss the management board by a vote of no confidence. However, even if it does so it is ultimately left for the supervisory board to decide on a discretionary basis whether to dismiss any or all members of the management board.¹⁴⁵ If the supervisory board eventually decides to dismiss a member of the management board, this decision can be challenged by the dismissed member in court.¹⁴⁶ To sum up, there is no direct way for the general meeting, i.e. a successful bidder, to enforce the replacement of the members of the management board. This can

141 Sec. 84 (1) sentence 5 AktG. As to *rolling contracts* in Britain see Chapter 3.3.5. at pp. 80.

142 *Peltzer*, Hostile Takeovers in der Bundesrepublik Deutschland?, ZIP 1989, 69, 74.

143 Sec. 84 (3) AktG. However, the dismissal-resolution does under the relevant labour law provisions, in particular sec. 626 BGB (serious cause), not automatically terminate the service contract of the director the result of which is that the dismissed director may still be entitled to his salary until the service contract expires.

144 Sec. 84 III AktG. For details see *Hüffer*, Aktiengesetz-Kommentar, § 84 Rn. 38, 39.

145 *Hauschka/Roth*, Übernahmeangebote und deren Abwehr im deutschen Recht, AG 1988, 181, 188; *Daum*, Die unkoordinierte Übernahme, p. 106.

146 Bundesgerichtshof BGH WM 1981, 759; *Hüffer*, Aktiengesetz-Kommentar, § 84 Rn. 33.

only be achieved with the help of the supervisory board. It is therefore of utmost importance to a bidder to win control of the supervisory board.

(2) The Supervisory Board

The supervisory board has the general duty to oversee the management of the stock corporation, but is not concerned with the day-to-day business.¹⁴⁷ In addition, the Stock Corporations Act provides for a number of specific powers and duties and the articles may confer further powers on the supervisory board as long as this does not conflict with the exclusive managerial tasks of the management board. The articles may, for instance, require approval by the supervisory board of certain transactions, like the acquisition of another company. Most importantly, as has already been pointed out the supervisory board is responsible for the appointment and removal of members of the management board.

(a) Appointment and Removal of the Members of the Supervisory Board

Pursuant to the Stock Corporations Act, the members of the supervisory board are elected by ordinary resolution by the shareholders in general meeting for a maximum period of five years.¹⁴⁸ Staggered terms of office are possible.¹⁴⁹ The general meeting is empowered to dismiss the members of the supervisory

147 Sec. 111 AktG.

148 Sec. 102 AktG.

149 See *Hauschka/Roth*, *Übernahmeangebote und deren Abwehr*, AG 1988, 181, 187.

board they elected.¹⁵⁰ However, such a resolution will normally require a three-quarter majority of the capital represented at the general meeting.¹⁵¹ The articles may allow for a greater or lesser majority. In practice, most of the listed stock corporations have modified their articles so that a simple majority suffices to remove the supervisory board,¹⁵² but this may well change if takeovers were to become more frequent in Germany. Unlike the removal of the management board, a sufficient or just cause is not required for the dismissal of a member of the supervisory board. The remuneration of the supervisory board members is either determined by way of a provision in the articles or a resolution of the general meeting.¹⁵³

This fairly clear picture is complicated and modified by the law concerning employee representation. Additionally, special appointment rights may be granted to certain shareholders.

(b) Employee Representation

The law regarding employee representation is complex and somewhat unmethodical. Only a basic review of the facts most relevant to a potential bidder will be given here.¹⁵⁴ The law is contained in a number of different acts outside the Stock Corporations Act.

150 Sec. 103 AktG.

151 Sec. 103 AktG.

152 *Otto*, Obstacles to foreigners are nothing but a myth, *Financial Times*, 20 February 1991.

153 Sec. 113 AktG.

154 A good review provide *Martens*, Das Recht der unternehmerischen Mitbestimmung, JuS 1983, 329 and *Hadden*, Employee Participation - What Future for the German Model?, *Company Lawyer*, Vol. 3, No. 6, p. 250 (1982).

(aa) Coal and steel industry with more than 1.000 employees

Employee representation on supervisory board level was first introduced in the coal and steel industry by the Coal and Steel Co-Determination Acts 1951 and 1956 (Montan-Mitbestimmungsgesetz). Under these provisions a supervisory board normally consists of 11 members, five of which are selected by the shareholders and five by the employees.¹⁵⁵ The eleventh member remains neutral. He is an agreed candidate selected jointly by both the shareholder and the employee representatives of the board.¹⁵⁶ Once selected all members of the supervisory board are elected by the general meeting. Because of this selection process, complete parity between the two major groups of the supervisory board exists and the vote of the neutral member will often be decisive.¹⁵⁷ The employee representatives can be removed by a resolution of the general meeting only if the employees propose to do so.¹⁵⁸ The neutral member can only be dismissed by court order if a sufficient cause exists.¹⁵⁹ For a successful bidder this means in practice that he will normally only be able to dismiss five out of eleven supervisory board members. Consequently, he is dependent upon the co-operation of either the neutral member or at least one member of the employee representatives to achieve the all important replacement of the members of the management board. Thus, as far as the steel and

155 Sec. 4 Montan-MitbestG 1951. Where corporate groups in the coal and steel sector are concerned, sec. 5 (1) of the Montan-Mitbestimmungsergänzungsgesetz 1956 applies (15 supervisory board members, 7 shareholder representatives, 7 employee representatives, 1 neutral member).

156 Sec. 8 Montan-MitbestG 1951.

157 For details see *Konzen*, Paritätische Mitbestimmung im Montanbereich, AG 1983, 289.

158 Sec. 11 Montan-MitbestG 1951, Sec. 103 AktG.

159 Sec. 11 (3) Montan-MitbestG 1951.

coal industry is concerned, the prospects of a hostile bidder winning effective control over the two corporate boards look rather bleak.

(bb) Stock corporations with less than 2.000 employees outside the coal and steel industry

Pursuant to the Works Constitution Act 1952 (Betriebsverfassungsgesetz 1952) at least one-third of the members of the supervisory board must consist of employee representatives.¹⁶⁰ Hence, the shareholder representatives retain the absolute majority of seats. In this category employee representation might be annoying, but it does not constitute a barrier to a successful bidder gaining control over the corporate boards. The supervisory board must have at least three members. The maximum number permitted by the Stock Corporations Act varies from 9 to 21 members depending on the capital of the company.¹⁶¹

It should be noted that in 1994 an amendment to the relevant Works Constitution Act 1952, designed to increase the popularity of stock corporations, abolished any form of mandatory employee representation on supervisory boards of newly floated stock corporations with less than 500 employees.¹⁶² Existing stock corporations with less than 500 employees are not affected, though.

160 Sec. 76 BetriebsVerfG.

161 Sec. 95 AktG.

162 Sec. 76 (4) BetriebsVerfG. See also Chapter 2 and *Kindler*, Die Aktiengesellschaft für den Mittelstand, NJW 1994, 3041, 3045.

(cc) Stock corporations with more than 2.000 employees outside the coal and steel industry

According to the Co-Determination Act 1976 (Mitbestimmungsgesetz 1976) half the members of the supervisory board must consist of employee representatives in this category.¹⁶³ The employee representatives are elected by the employees and may only be removed by them.¹⁶⁴ The number of supervisory board members depends on the size of the company and ranges from 12 to 20.¹⁶⁵ However, unlike the coal and steel industry, parity is not fully achieved because the chairman of the supervisory board, who is, if no other agreement is reached, elected by the shareholder representatives of the board, has a casting vote.¹⁶⁶ Thus, although equal in number, the shareholder representatives can - if all members are present - always secure a majority in the supervisory board. Again, employee representation in these companies may be considered a "nuisance" by a successful bidder; it does not deter it, however, from exercising effective control over the corporate boards.

(c) Special Appointment Rights

Special rights to appoint up to one-third of the shareholder representatives of the supervisory board may be granted by the articles to certain shareholders.¹⁶⁷ Supervisory board members appointed in that way may only be removed by the shareholders

163 Sec. 7 MitbestG 1976.

164 Sec. 31 MitbestG 1976.

165 Sec. 7 MitbestG 1976.

166 Sec. 27, 29 MitbestG 1976.

167 Sec. 101 AktG. *Henle*, Defences to Corporate Takeover in Germany, [1994] ICCLR 122, 126; *Immenga/Hellberg*, Corporate Takeovers through the public market, p. 30.

having the appointment right.¹⁶⁸ Consequently, where such rights exist together with the law regarding employment representation they may easily prevent a bidder from gaining control of the supervisory board.

(3) Summary

Compared to English company law removing and appointing the members of the two corporate boards in Germany is generally speaking a major operation not easily achievable on a short-term basis. However, depending on the company's articles, its field of business and size, the removal requirements and the scale of employment representation on the supervisory board differ widely. Apart from the coal and steel industry, employee representation cannot prevent an successful bidder from gaining control of the corporate boards, though it makes German companies certainly less attractive to a foreign bidder not used to such a complex system of corporate governance. The main hurdle is the 75 per cent majority normally required to dismiss the shareholder representatives of the supervisory board. However, the articles of large companies may and often do stipulate a lower threshold. Yet, if special appointment rights are granted to particular shareholders, the bidder is in companies with more than 2.000 employees unlikely to succeed. Once the bidder controls the supervisory board, the dismissal and reappointment of the management board does not constitute a great problem. In any case, a very thorough analysis of the articles of the potential target company and the employment law applicable is essential in order to assess the difficulties a bidder might face. Although it does in most cases not seem impossible to overcome these obstacles, provided the bid is very carefully planned and

168 Sec. 103 AktG.

handled, the statement that the mentioned obstacles are “*nothing but a myth*”¹⁶⁹ appears exaggerated to say the least. In general, the two-tier board system together with the absence of a provision equivalent to section 303 of the Companies Act 1985 on the one hand and the extensive employee representation on the other hand complicate takeovers and give German stock corporations some scope for the erection of barriers. Since the obstacles mentioned here represent a fundamental part of German company and labour law and are not specifically erected with an intent to hamper (foreign) takeovers, changes are not likely in this respect.

4.2.3. The Role of the Banks

To itemize banks as takeover barriers may be surprising to a British reader. Indeed, given the enormous fees involved in Britain,¹⁷⁰ British merchant banks are among the main beneficiaries and promoters of takeovers and, thus, quite the opposite of a barrier.

In order to understand why and in what way German banks are likely to impede non-agreed takeover bids, it is necessary to examine the role of banks in the German economy first. The unique position of German banks mainly derives from four factors.¹⁷¹

169 Otto, Obstacles to foreigners are nothing but a myth, *Financial Times*, 20 February 1991.

170 See, for example, *Times*, 11 January 1995: Trafalgar faces £60 million bid fees. *Financial Times*, 8 March 1995: the Glaxo/Wellcome bid expenses were expected to be around £100 million. Glaxo, advised by Lazard Brothers, had estimated its expenses at £77 million, of which £30 million were fees, and the rest stamp duty. Wellcome, advised by Barings and Morgan Stanley, was expected to pay between £20 to £30 million. See also *Financial Times*, 24 January 1996: the Granada/Forte battle incurred £140 million in fees and costs. See also the critical article in the *Guardian*, 30 January 1995: Merger mania is madness.

171 See Raiser, Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften, NJW 1996, 2257; Maier-Reimer, Protection Against Hostile Takeovers in Germany: Banks and Limitations on Voting Rights, p. 242 et seq. For an analysis including an empirical study see ZBB-Dokumentation, Die Macht der Banken - Anhörung im Bundestag, ZBB 1994, 69-100.

First, there is the traditional universal banking system which normally leads to a “*house-bank relationship*” between a bank and its client.¹⁷² Unlike British banks which are usually either retail banks, wholesale banks, merchant banks or security firms and provide more or less specialized services only,¹⁷³ German banks are not normally specialized, but offer all sorts of financial services one can think of.¹⁷⁴ They may well be likened to a financial supermarket.¹⁷⁵ The fact that German companies are able to receive all financial services they possibly need from one bank normally leads to the so called house-bank relationship with one particular bank. In other words, a close long-term relationship with symbiotic features evolves between the bank and the company. Since the financing of German companies depends heavily on bank credits,¹⁷⁶ it is as important for the bank to be well informed about the company’s affairs as it is for the company to enjoy the bank’s goodwill and trust. Shopping around for financial services has not been a feature of corporate finance in Germany although there are indications that this may change in future.¹⁷⁷

Secondly, this already close relationship between house-bank and company is often intensified by directorates on the supervisory board of the client-company granted to representatives of the house-bank which affords the bank with complete insight into the company’s affairs. The Monopolies Commission (Monopolkommission) revealed that in 1988 the nine biggest banks held ninety-four seats on the supervisory boards of ninety-six of the

172 *Baums*, Banks and Corporate Control in Germany, p. 267, 270; *Daum*, Die unkoordinierte Übernahme, p. 242. *Hopt*, European Takeover Regulation, p. 165, 169. A very good analysis regarding potential conflicts of interest arising from the universal banking system presents *Peltzer*, Die Rolle der Banken bei Unternehmensveräußerungen, ZIP 1991, 485. *Werner*, Probleme feindlicher Übernahmen, p. 19.

173 *Prest/Coppock’s*, The UK Economy, p. 79 et seq.

174 For an enumeration of the business carried out by banks see § 1 Kreditwesengesetz (Banking Act 1993).

175 *Hopt*, European Takeover Regulation, p. 165, 169.

176 See Chapter 2 at pp. 17.

177 *Baums*, Banks and Corporate Control in Germany, p. 267, 270.

biggest 100 companies in Germany! The leading *Deutsche Bank* alone held thirty-five of these seats.¹⁷⁸ A survey of the exclusive DAX-30-Index companies unveiled that 25 per cent of the non-employee supervisory board members were bank representatives.¹⁷⁹ These frequent personal interlocks between leading banks and blue-chip German companies have resulted in a close-knit network of establishment figures - something rather well known in Britain.

Thirdly, the banks regularly hold considerable stakes in the major companies they have business with which further strengthens their influence.¹⁸⁰ The table contained in APPENDIX 4 showing the stakes held by German banks in listed German Stock Corporations illustrates this point well.¹⁸¹

Last but not least, banks usually act as depositaries for small investors and administer and vote their shares.¹⁸² Unlike Britain, proxy voting by the management of a stock corporation is not admissible in Germany.¹⁸³ Whereas in Britain proxies may unduly increase the board's power they most certainly do so in respect of banks in Germany.¹⁸⁴

Looking back at these four factors - house-bank relationships, personal interlocks, stakes, and proxy votes - it is evident how

178 For further details see *Baums*, Banks and Corporate Control in Germany, p. 267, 275. As to a characterisation of the Deutsche Bank see *Economist*, 22 June 1991: "...Rich, aloof, secretive, it has been admired for its skill, but often attacked, even feared, as a behind-the-scenes puller of the strings..."

179 *Raiser*, Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften, NJW 1996, 2257, 2258 with further details and references.

180 *Baums*, Banks and Corporate Control in Germany, p. 267, 271.

181 For detailed information see AG-Report, Fragen im Bundestag zu den Bankbeteiligungen, AG 1995, R 506-507. *Adams*, Die Usurpation von Aktionärsbefugnissen mittels Ringverflechtung in der "Deutschland AG", AG 1994, 148, 153.

182 Sec. 135 AktG and the provisions of the Depotgesetz 1937. *Baums*, Banks and Corporate Control in Germany, p. 267, 272.

183 Sec. 136 II AktG; *Hüffer*, Aktiengesetz-Kommentar § 134 Rn. 25.

184 *K. Schmidt*, Gesellschaftsrecht, § 28 IV p. 717; *Baums*, Banks and Corporate Control in Germany, p. 267, 272.

powerful the position of the large banks in both the German economy as a whole and in respect of their clients is. Because of those close house-bank relationships, a hostile bid for the client company is very likely to be rejected by the bank too. If the house-bank co-operated with the bidder, it would risk to lose its old client to another bank. Besides, hostile takeovers as a means of acquiring corporate control are still viewed with distaste by the conservative German banking establishment.¹⁸⁵ The former president of the *Deutsche Bank*, who was murdered by left-wing terrorists in 1989, *Alfred Herrhausen*, once coined the phrase, that “takeovers are a wrong track of capitalism”.¹⁸⁶ Hence, if, for example, an unwelcome foreign company attempted to win control over a large German stock corporation, it would most probably not only have to put up with defensive measures installed by the target company itself but also with the house-bank voting its own shares and, more importantly, the proxy-shares of its clients against the bidder.¹⁸⁷ If the house-bank is one of the big three private banks - *Deutsche Bank*, *Dresdner Bank* and *Commerzbank* - which is not unlikely if a large stock corporation is concerned, the number of shares voted by the bank could be very considerable. This position is further strengthened by the usually relatively low level of shareholder participation in general meetings.¹⁸⁸ Although shareholders may instruct the depository bank on how to vote their shares,¹⁸⁹ private investors normally do not bother. Whether this habit would change in case of a takeover

185 See *Werner*, Probleme feindlicher Übernahmen im Aktienrecht, p. 7 et seq. *Economist*, 4 July 1992; *Hopt*, European Takeover Regulation, p. 165, 169.

186 *Werner*, Probleme feindlicher Übernahmen im Aktienrecht, p. 7.

187 *Adams*, Die Usurpation von Aktionärsbefugnissen mittels Ringverflechtung in der “Deutschland AG”, AG 1994, 148, 155.

188 For an empirical study see *ZBB-Dokumentation*, Die Macht der Banken - Anhörung im Bundestag, ZBB 1994, 69, 76. The following figures relate to 1992: *BASF*: 50,3 %; *Bayer*: 50,1 %; *Conti-Gummi*: 52,8 %; *Daimler*: 79,0 %; *Hoechst*: 71,3 %; *Hoesch*: 87,6 %; *Mannesmann*: 37,2 %; *Schering*: 35,9 %; *Siemens*: 50,0 %; *Thyssen*: 68,2 %; *VEBA*: 51,0 %; *VW*: 34,9 %.

189 Sec. 135 AktG.

battle taking place seems rather doubtful.¹⁹⁰ If, as is often the case, the voting rights exercisable by one shareholder are restricted to, say, 5 per cent, the situation becomes even more difficult for a bidder.¹⁹¹ Whereas the bidder as a single shareholder cannot exercise more than 5 per cent of its own shares, the bank can vote up to 5 per cent for each of its proxy-clients for it is not considered a single shareholder in its capacity as proxy. In these cases, banks are de facto by far the most important "shareholders".

To sum up, in the present "corporate climate" in Germany it is likely that a hostile bid would be opposed by the relevant house-bank(s) of the target company. For the reasons given, this would result in a very serious barrier for any bidder.¹⁹² Although the power of the banks has been widely criticized in recent years, the present system is part of German corporate culture and not easy to change. While the present system clearly hampers a "market for corporate control", as it is known in Britain, and therefore constitutes a barrier, the German system has its advantages in terms of corporate governance too which is why many oppose changes to the present structure. A major argument in favour of the German system is that the heavy involvement of the often very competent banks, which have a natural interest in their clients prospering, helps management, ensures that difficult (financial) reconstructions go through, and guarantees a higher overall measure of stability which contributes to the success of the economy as a whole. However, in the face of growing international competition and the desire to make the German stock market more attractive to (foreign) investors, it is likely that the banks will lose some of their power in the long run. A number of proposals to that end have been made, including a limitation of the banks' right to hold stakes in non-banking

190 Contrary: *Otto*, Obstacles to foreigners are nothing but a myth, *Financial Times*, 20 February 1991.

191 See in detail Chapter 4.3.1. at pp. 157.

192 The same conclusion reaches *Adams*, Die Usurpation von Aktionärsbefugnissen mittels Ringverflechtung in der "Deutschland AG", AG 1994, 148, 153.

corporations and a restriction of the banks' function as depositaries.¹⁹³

4.2.4. Availability of Corporate Information

The availability of corporate information is one of the essential pre-conditions without which a market for corporate control cannot operate. The following subchapters will consider the accessibility of the target's articles, the availability of financial information, and the identification of its shareholders.

(1) The Articles

Although there is no centralised Companies Registration Office as it exists in England, Scotland, and Northern Ireland,¹⁹⁴ Commercial Registers (Handelsregister) are located at every District Court (Amtsgericht) in Germany.¹⁹⁵ Thus, several hundred of them are spread all over the country.

Stock corporations are required to file their articles at the time of the initial registration and whenever amendments are made with the competent Commercial Register,¹⁹⁶ within whose jurisdiction they have their corporate seat. The corporate seat of a stock corporation is determined by the articles subject to the qualification that it must either be the location of the company's headquarters or a place

193 As to further references to these recent developments see *Raiser*, Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften, NJW 1996, 2257, 2258 et seq.; *Baums*, Vollmachtstimmrecht der Banken - Ja oder Nein?, AG 1996, 11 et seq. For a balanced review of these issues see also *Peltzer*, Empfehlen sich gesetzliche Regelungen zur Einschränkung des Einflusses der Kreditinstitute auf Aktiengesellschaften?, JZ 1996, 842 et seq. and *Peltzer*, Die Vertretung der Aktionäre in Hauptversammlungen von Publikumsgesellschaften, AG 1996, 26 et seq.

194 Sec. 704 CA 1985.

195 Sec. 8 HGB (Handelsgesetzbuch = Trade Act). For details see the Commercial Register Rules 1937 (Handelsregisterverordnung).

196 Sec. 36, 37, 181 AktG.

where the company has at least a production unit.¹⁹⁷ Documents submitted to the Commercial Register are open for inspection by the public without any further qualifications.¹⁹⁸

To identify the competent Commercial Register is not a problem: Stock corporations are required to state on their business letters where the corporate seat is located, which the competent Commercial Register is, and the registration number under which the company's articles are to be found in the respective Commercial Register.¹⁹⁹ Moreover, the names of the management board-members as well as that of the chairman of the supervisory board have to be specified. Hence, it should not prove difficult for a potential bidder to obtain the target's articles at little to no cost.

(2) Financial Information

Apart from the share price, which reflects to some extent the company's performance, financial information basically means accounting information. The implementation of the Fourth²⁰⁰ and Seventh²⁰¹ Directive had a radical effect on German accounting, the details of which are beyond the scope of this work.²⁰²

As in Britain, companies are categorised. Publicly listed stock corporations are deemed to be large companies, i.e. the most stringent accountancy rules apply.²⁰³

197 Sec. 5 AktG.

198 Sec. 9 HGB.

199 Sec. 80 (1) AktG. The situation is identical with respect to limited companies: sec. 35a GmbHG. These provisions go back to Article 3 of the First Council Directive 68/151/EEC of 9 March 1968, O.J. L 65/8.

200 78/660; [1978] O.J. L222/11. Implemented in the U.K. by the Companies Act 1981.

201 83/349; [1983] O.J. L193/1. Implemented in the U.K. by the Companies Act 1989.

202 See *Schmidt*, Gesellschaftsrecht, § 29 IV, p. 759 et seq.

203 Sec. 267 HGB.

A stock corporation has to file its year end balance sheet together with the related profit and loss account and notes thereto plus the directors'²⁰⁴ and the auditors' report with the relevant Commercial Register. Of particular interest to a potential bidder could be the directors' report, which must provide a fair review of the development of the business.²⁰⁵ Again, all information filed with the Commercial Register is publicly accessible.²⁰⁶ Because of the detailed provisions in the Accounting Directive, the differences between Britain and Germany in this respect seem rather minor.

(3) Shareholder Identification

The predominant use of bearer shares in Germany has been pointed out in different contexts before.²⁰⁷ It is obvious, that the anonymity afforded by bearer shares is an obstacle to the identification of shareholders. The knowledge of the ownership structure is, however, an important factor in assessing the prospects of a public offer. If it happens to be the case that (some) registered shares are issued,²⁰⁸ the register of members may be inspected at the company's registered office by any member free of charge.²⁰⁹

The severity of the barrier here discussed has been reduced - as far as listed stock corporations are concerned - since the introduction of the Securities Trading Act in January 1995, which lessened the disclosure thresholds from 25 per cent to only 5 per cent.²¹⁰

204 In a stock corporation normally prepared by the management board (Vorstand).

205 Sec. 264, 289 HGB.

206 See Chapter 4.2.4. (1) at pp. 148.

207 See Chapter 4.1.2. at pp. 122.

208 Sec. 10 AktG.

209 Sec. 67 AktG.

210 See Chapter 4.1.2.(2) at pp. 125 and APPENDIX 3.

However, shareholders holding less than 5 per cent may only be contacted through banks, if the banks act as depositaries,²¹¹ or public media announcements. If a notice of the offer is published in a specific quasi-official publication, the *Wertpapiermitteilungen III*, banks acting as depositaries are under No. 16 of the *Sonderbedingungen für Wertpapiergeschäfte*²¹² obliged to inform their clients holding shares of the target of the offer. Although it is in respect of those shareholders using banks as depositories not possible for a bidder to indentify them by name, it is possible to contact them “anonymously” through the banks.

To sum up, shareholder identification remains a somewhat difficult issue in Germany, albeit it should not be considered an absolute barrier to a takeover.²¹³

4.2.5. The Law Governing Groups of Companies

The German Stock Corporations Act comprises a distinct body of rules governing the relationship between holding companies and subsidiaries (see APPENDIX 2).²¹⁴ Although this so called “*Konzernrecht*” does not impede the acquisition of a controlling stake, it can complicate the post-acquisition integration of the newly acquired stock corporation into the bidder’s empire and in so far constitute an indirect barrier to a successful takeover.²¹⁵ Moreover, the concept of a special law of groups has no direct equivalent in

211 To the role of banks in this context see Chapter 4.2.3. at pp. 143.

212 *Sonderbedingungen für Wertpapiergeschäfte* reproduced in WM 1995, 362 et seq. For a discussion see *Kümpel*, Die neuen Sonderbedingungen für Wertpapiergeschäfte, WM 1995, 137, 143.

213 As to the disclosure of members present at a general meeting see Sec. 129 Akt and Article 29 of the proposed 5th Directive.

214 Sec. 291-328 AktG. A translations of these provisions can be found in *Hopt* (ed.), *Groups of Companies in European Laws*, 1982, p. 265-295.

215 *Hopt*, *European Takeover Regulation*, p. 171.

English law²¹⁶ and a British bidder might therefore not be fully aware of the implications these rules have in practice.

The aim of the German law of groups mainly is to protect minority shareholders in and creditors of the subsidiary company from the particular hazards which come with dependency from another company.²¹⁷ It has been pointed out earlier that the absence of a mandatory bid requirement results in companies often holding just as large a stake as is necessary to control the target company effectively, and the need for a special law of groups is therefore greater than in Britain.²¹⁸

Corporate groups in Germany may be based either on some form of control contract,²¹⁹ which is to some extent favoured by tax law,²²⁰ or on the holding of a controlling stake, the so-called de facto group.

(1) Contract-based Groups

The conclusion of a control contract and/or profit transfer contract between the holding and the subsidiary company as provided for in section 291 of the Stock Corporations Act leads to a complete dependency of the subsidiary company and grants the holding company the right to give binding instructions which may be detrimental to the interests of the subsidiary as long as the parent company is acting in the interest of the group as a whole.²²¹ Thus, in

216 Pennington, *Company Law*, p. 748; *Prentice*, *Groups of Companies in European Laws*, p. 99; Schmitthoff, *The wholly owned and controlled subsidiary*, [1978] JBL 218.

217 For an outline of the German law of groups in English see *Immenga*, *The Law of Groups in the Federal Republic of Germany*, p. 85-121.

218 See Chapter 3.2.1. at pp. 67.

219 As to the different types of contracts see Sec. 291, 292 AktG.

220 *Emmerich/Sonnenschein*, *Konzernrecht*, § 10 I.

221 Sec. 308 AktG. For details see *Emmerich/Sonnenschein*, *Konzernrecht*, § 18.

this kind of situation the target company is fully integrated and the bidder has achieved its aim. However, coming to this point is not an easy task for a bidder, and the price to pay is considerable. A control or profit transfer contract requires the approval of 75 per cent of the capital represented in the general meetings of the respective companies and needs to be filed with the Commercial Register.²²² The requirement of a consideration not being a concept of the civil law, there are no provisions regarding this matter. However, the law undertakes to protect the minority shareholders in the subsidiary and its creditors in various ways, of which only the most important are mentioned here.

First, in the interest of the subsidiary's creditors the holding company must settle any losses the subsidiary runs up throughout the financial year.²²³

Secondly, a fixed dividend must be guaranteed to the minority shareholders in the subsidiary based on the subsidiary's record previous to the control and/or profit transfer contract.²²⁴ The exact amount payable to the minority shareholders may be reviewed by the courts on the application of any minority shareholder.

Thirdly, a control or profit transfer contract must contain a clause granting any minority shareholder the right to be bought out for a fixed price.²²⁵ Again, if a shareholder is not satisfied with the price offered, he may bring the issue before the courts - which shareholders in practice often do.

222 Sec. 294 AktG.

223 Sec. 302 AktG.

224 Sec. 304 AktG.

225 Sec. 305 AktG.

(2) De Facto Groups

Where a de facto group exists, i.e. a group not based on a contract but on a controlling stake, the holding company must, unlike the parent company in a contract based group, not use its influence - in whatever way it is exerted - to force the subsidiary into any detrimental transactions or other disadvantageous steps unless it takes precautions to compensate the subsidiary for the losses incurred within the financial year.²²⁶ Unless a control contract is concluded, the management of the subsidiary is - at least in theory - fully independent and not obliged to follow any instructions given to it by either its general meeting or, indeed, anybody else.²²⁷ It has to act in the best interests of the subsidiary company and not the group. If the holding company exerts a detrimental influence without making good the losses ensuing, the holding company²²⁸ itself as well as the members of its boards²²⁹ may be liable for the damages suffered by the subsidiary because of the detrimental influence exercised. The management of the subsidiary may also be liable because of a contravention of its duty to act in the best interests of the (subsidiary) company.²³⁰ Both the subsidiary company itself and, more importantly, its shareholders may instigate court procedures against the holding company and its management to claim damages.

Moreover, if the de facto influence wielded by the holding company reaches a degree where the subsidiary is - contrary to the principle of independence of management²³¹ - permanently more or less run like a mere branch of the holding company,²³² the holding

226 Sec. 311 AktG.

227 Sec. 76 AktG. *Emmerich/Sonnenschein*, Konzernrecht, § 19 I; *Immenga*, The law of groups, p. 85, 107.

228 Sec. 317 AktG.

229 Sec. 318 AktG.

230 Sec. 93 AktG.

231 Sec. 76 AktG.

232 So-called "qualifizierter faktischer Konzern".

company has according to the majority opinion to settle all losses the subsidiary incurs throughout the financial year regardless of any specific and identifiable detrimental actions forced upon it by the holding company (qualified de facto group). Since such a situation of total de facto dependency would amount to a situation by and large similar to that under a control or profit transfer contract, the majority opinion in Germany advocates that consequently these rules should apply by way of analogy in order to prevent a circumvention of the stricter shareholder and creditor protection guaranteed by these rules. Hence, the consequences for a successful bidder exercising the described strong influence on the target can be drastic.

Generally speaking, however, it is very difficult for the minority shareholders, with whom as potential plaintiffs lies the burden of proof, to assess what is going on in the respective boardrooms and whether any detrimental influence is exercised by the holding company.²³³ To address this problem the law requires the management board of the subsidiary to draw up on an annual basis a detailed so-called *dependency report* specifying any transactions between the respective companies and any steps taken by the subsidiary at the instance of the holding.²³⁴ This report is examined by the subsidiary's auditors, but for reasons of business secrecy it may not be inspected by shareholders or creditors²³⁵ which has led to the general belief that the dependency report is of little use in practice. Generally, it is widely acknowledged that the enforcement of the rules concerning de facto groups leaves much to be desired.²³⁶ As has been stated, their enforcement mainly relies upon either the subsidiary's management or the shareholders bringing actions for damages against the holding company. The subsidiary's

233 *Emmerich/Sonnenschein*, Konzernrecht, § 21 II; *Immenga*, The law of groups, p. 85, 108.

234 Sec. 312 AktG.

235 Sec. 313 AktG.

236 *Emmerich/Sonnenschein*, Konzernrecht, § 20 IV 1; *Immenga*, The law of groups, p. 85, 108. *K. Schmidt*, Gesellschaftsrecht, § 31 IV 1, p. 802.

management, however, if appointed by the holding company, will not normally act against the holding company, and individual shareholders usually lack the evidence and the considerable financial means necessary to bring such an action about. Enforcement against a foreign holding company looks even more difficult.²³⁷ Nevertheless, a potential foreign bidder must be aware of the obligation imposed on it by the law of groups.

(3) Summary

To sum up, although the German law of groups is far too complex to be fully considered in this chapter, the point here made is that these rather complicated rules tend to restrict the integration of a stock corporation into a corporate group in favour of the protection of minority shareholders and creditors of the subsidiary. Full integration is only possible if both parties enter into a control and/or profit transfer contract. However, even if the majorities required for this can be secured, it has been demonstrated that such a contract has its drawbacks too. Similar to the law concerning employee representation, the law of groups does not prevent a bidder from acquiring control, but it renders corporate governance more difficult and probably makes German stock corporations less attractive in the eyes of potential foreign bidders.

4.3. Protective Measures in Advance of a Bid

Given the structural barriers inherent in German law, it is obvious that there is comparatively little need for additional defensive measures. This chapter will be confined to those “poison pills” of at

²³⁷ *Emmerich/Sonnenschein, Konzernrecht*, § 8 III 2.

least some practical relevance in the present corporate climate in Germany. Two defensive measures, namely staggered terms of office for the members of the supervisory board²³⁸ and special appointment rights²³⁹, have already been examined in the pertinent context of the respective structural barriers.

4.3.1. Restrictions on Voting Rights

Restrictions on voting rights have a long history in Germany. They were widespread during the 1920s, provoked mainly by the general fear of “*foreign infiltration*”.²⁴⁰ Their use was severely restrained, however, when the 1938 amendment to the Stock Corporations Act 1937 made the introduction of such restrictions conditional upon ministerial approval. Yet, this condition was abolished by the Stock Corporations Act 1965²⁴¹ and voting restrictions became fashionable again in the mid 1970s when after the “*oil-crisis*” in 1973/74 oil-exporting Arab states such as Kuwait and Iran bought large stakes in German blue-chip stock corporations, such as *Daimler Benz* and *Krupp*, which was - rightly or wrongly - commonly perceived as a threat to national security.²⁴² The latest wave of voting restrictions came in the late 1980s when the managements of large listed stock corporations with a widely dispersed shareholder structure, alarmed by events in neighbouring European countries and Germany itself, suddenly realised the possible threat of takeovers.²⁴³ Nowadays voting restrictions are the

238 See Chapter 4.2.2.(2)(a) at pp. 137.

239 See Chapter 4.2.2.(2)(c) at pp. 141.

240 *Baums*, Höchststimmrechte, AG 1990, 221, 239.

241 Sec. 134 AktG.

242 *Haberland*, Aktienrechtliche Maßnahmen zur Abwehr unerwünschter Beteiligungen, BB 1975, 353.

243 *Martens*, Stimmrechtsbeschränkung und Stimmbindungsvertrag im Aktienrecht, AG 1993, 495; *Zöllner/Noack*, One share - one vote? AG 1991, 117.

German standard “poison pill”, introduced by companies like *Asko*, *BASF*; *Bayer*, *Continental*, *Deutsche Babcock*, *Deutsche Bank*, *Dresdner Bank*, *Dykerhoff*, *Henkel*, *Hoesch*, *Mannesmann*, *Veba* and *Volkswagen*, to mention but a few illustrious names.²⁴⁴

As has been explained earlier, voting right limitations restrict the number of votes an individual shareholder may exercise.²⁴⁵ The most common limit chosen is 5 per cent. To introduce a voting right restriction into the articles of a stock corporation a 75 per cent majority of the capital represented in the general meeting is required.²⁴⁶ The articles may provide that shares held by a nominee or a controlled, dependent, or affiliated company must be aggregated to the holding.²⁴⁷

The economic effect of a restriction on the exercisable votes is that investors are strongly discouraged to acquire a stake exceeding the percentage of the voting right limitation. A point often made to justify the introduction of voting right restrictions is that they, apart from scaring off corporate raiders, protect small investors from becoming locked-up minority shareholders deprived by a domineering majority shareholder.²⁴⁸ However, this is only part of the picture. As one would think, there is clear evidence that the introduction of a voting right restriction affects the share price adversely because the company becomes less attractive to large investors.²⁴⁹ The drop of the share price, however, is certainly not in the interest of small investors and neither is depriving them of the benefits of an attractive takeover offer. In fact, the interests of small investors often seem to play the least role in the introduction of a voting right restriction. What all too often seems to be behind it can -

244 For details see *Baums*, *Höchststimmrechte*, AG 1990, 221 footnote 6.

245 See Chapter 4.2.3. at pp. 143.

246 Sec. 134, 179 AktG.

247 Sec. 134 AktG.

248 *Martens*, *Stimmrechtsbeschränkung und Stimmbindungsvertrag*, AG 1993, 496.

249 According to *Baums*, *Höchststimmrechte*, AG 1990, 221, 226 the average share share price drop is about 4 per cent.

with only slight exaggeration - be called an unholy alliance between the incumbent management and the depositary banks.²⁵⁰ The management, especially the members of the supervisory board who are appointed and dismissed by the general meeting, favour the introduction of voting right restrictions because in the absence of powerful shareholders the balance of power is further shifted in their direction and guarantees almost complete independence from shareholder control and pressure.²⁵¹ Quite similar are the interests of the banks. In their capacity as proxies they are not considered to be shareholders which allows them to vote for each client the shares up to the voting limit!²⁵² This leads to the banks being by far the most influential voters in these companies, their proxies alone often representing the "majority". Since any bidder would acquire vast numbers of shares from small investors in a takeover, it is inevitable that the banks lost proxies which reduced their influence.²⁵³ This is, of course, reason enough for them to oppose takeover bids and to vote in favour of the introduction of voting right limitations.

Concerning the introduction of voting right limitations there is, hence, a clear conflict of interest regarding the management of the company and the banks. Some academic writers have called for a change of law and the abolition of voting right restrictions, which appears to be the preferable view.²⁵⁴ The majority opinion,²⁵⁵ however, maintains that voting right restrictions are essential to scare

250 Critical too *Adams*, *Unbehinderte Übertragbarkeit*, AG 1990, 243, 250; *Baums*, *Höchststimmrechte*, AG 1990, 221, 227 et seq.

251 See Chapter 4.2.2.(2)(a) at pp. 137.

252 See Chapter 4.2.3. at pp. 143.

253 *Adams*, *Höchststimmrechte, Mehrfachstimmrechte und sonstige wundersame Hindernisse*, AG 1990, 63 and *Adams*, *Unbehinderte Übertragbarkeit*, AG 1990, 243, 250; *Baums*, *Höchststimmrechte*, AG 1990, 221, 227 et seq.

254 *Adams*, *Höchststimmrechte, Mehrfachstimmrechte und sonstige wundersame Hindernisse*, AG 1990, 63; *Baums*, *Höchststimmrechte*, AG 1990, 221, 227 et seq.

255 *Hüffer*, *Aktiengesetz-Kommentar*, § 134 Rn. 5; *Martens*, *Stimmrechtsbeschränkung und Stimmbindungsvertrag*, AG 1993, 496; *Zöllner/Noack*, *One share - one vote?* AG 1991, 117.

off destructive corporate raiders and there seems at present little prospect for a change of law in Germany.²⁵⁶

Although a bidder may try to circumvent the restriction legally by entering into shareholder agreements,²⁵⁷ *Pirelli's* example in the attempted *Continental* takeover showed that this may have disastrous consequences.²⁵⁸ Besides, depending on the shareholder structure this may not always be possible and in any case very difficult to organise for a foreign bidder. As many of the more important general meeting resolutions, in particular any change of the articles, require a twofold majority (majority of the votes *plus* 75 per cent of the share-capital represented concerning which the voting right restriction does not apply),²⁵⁹ by acquiring a blocking stake of 25 per cent of the share-capital a bidder may use this blocking power to force in the long run the incumbent management, who may not be ousted from office due the voting right limitation, to make concessions.²⁶⁰ Hence, restrictions on voting rights may not make a stock corporation completely bid proof, but they are an effective and widely used weapon in the German anti-takeover arsenal to make the post-acquisition integration of the target very difficult.

256 As to changes proposed by Art. 33 (2) of the draft 5th Directive see Chapter 5.2.2. at pp. 200.

257 *Baums*, Höchststimmrechte, AG 1990, 221, 225; *Martens*, Stimmrechtsbeschränkung und Stimmbindungsvertrag, AG 1993, 495, 496.

258 See Chapter 4.(2) at pp. 103.

259 Sec. 134 (1) sentence 6 and sec. 179 (2) AktG.

260 See in detail *Baums*, Höchststimmrechte, AG 1990, 221, 225.

4.3.2. Registered Shares with Restricted Transfer

Recent events, which will be discussed later, give reason to examine the use of registered shares in the context of takeover defences. Although the shares issued in Germany are predominantly in the form of bearer shares,²⁶¹ the Stock Corporations Act permits the issue of registered shares as well.²⁶² Moreover, the articles may make the transfer of registered shares conditional upon the consent of the company which, unless the articles stipulate otherwise, means that the management board has to make this decision.²⁶³ If the articles do not specify the grounds on which the transfer may be refused, the directors enjoy wide discretion. They are only bound by their duty to act in the best interests of the company.²⁶⁴ Rather untypical for German stock corporation law, but quite like the situation in English company law, much is left for the articles to determine in respect of transferability. However, both in Britain²⁶⁵ and Germany²⁶⁶ securities must be freely transferable if they are to be listed on a stock exchange. Yet, exceptions to this principle may be made by the competent authorities in the respective countries as long as the restricted transferability does not disturb the market. A direct comparison of the wording²⁶⁷ of the relevant provisions shows,

261 See Chapter 4.2.4.(3) at pp. 150.

262 Sec. 10 AktG.

263 Sec. 68 AktG.

264 Landgericht Aachen, ZIP 1992, 924; Hüffer, Aktiengesetz-Kommentar, § 68 Rn. 15. Henle, Defences to Corporate Takeover in Germany, [1994] 4 ICCLR 122, 124.

265 Rule 3.15 of the Yellow Book.

266 Sec. 5 Börsenzulassungsverordnung.

267 Rule 3.15 of the Yellow Book: *"In exceptional circumstances approved by the Exchange an applicant may take the power to disapprove the transfer of shares provided that the exercise of such power would not disturb the market in those shares."*

Sec. 5 II Nr. 2 Börsenzulassungsverordnung: *"Die Zulassungsstelle kann Aktien, deren Erwerb einer Zustimmung bedarf, zulassen, wenn das Zustimmungserfordernis nicht zu einer Störung des Börsenhandels führt."*

however, not only that the British drafting is more precise but also that the requirements are more stringent. Under the Yellow Book restricted transferability may only be allowed in “*exceptional circumstances*” whereas the German Admission Rules do not require this. In practice, restricted transfer of shares in Germany is often found in smaller non-listed stock corporations dominated by a family. However, for historical reasons insurance companies listed on the German stock exchanges frequently do have registered shares with restricted transfer.²⁶⁸ As the following example demonstrates, a hostile takeover of such an insurance company in Germany is - at best - extremely difficult.

In 1990/1991 the French insurance company *Assurances Générales de France* (AGF), in which the French government has a 75 per cent stake, tried to acquire a so-called blocking minority²⁶⁹ of little more than 25 per cent in the German *Aachener und Münchener Versicherungsgruppe* (AMB), whose capital consists mainly of registered shares, the transfer of which is conditional upon the management board’s consent.²⁷⁰ Having acquired a small stake already, AGF then wanted to acquire a further 17.6 per cent stake in AMB, consisting of registered shares with restricted transferability, from a Swedish insurance company which would have brought its holding beyond the 25 per cent blocking-threshold. However, pursuant to the power vested in them by the articles, the management board of AMB simply disapproved of this deal giving no further reasons. AGF challenged this decision unsuccessfully in court. It was held that it was perfectly legitimate for AMB to reject AFG on the grounds that it wanted to remain independent from

(= *The admissions authority may admit securities to listing provided the admission would not disturb the market.*)

268 *Otto*, Übernahmeveruche bei Aktiengesellschaften, BB Beilage 12/88, p. 6, footnote 55. Landgericht Aachen, ZIP 1992, 924, 925.

269 A number of important corporate decisions, like e.g. the amendment of the articles, need the approval of a 75 per cent majority in the general meeting. Thus, the holding of a blocking majority increases this shareholder’s influence considerably.

270 As to the details see Landgericht Aachen, ZIP 1992, 924 et seq.

foreign quasi-governmental influence. Furthermore, the wording of the court's decision suggests that because of the wide discretion vested in the management by the articles in this case that the decision would not have been different had the bidder not been owned by the French government, but private investors. This case, hence, highlights that where registered shares with restricted transferability exist, a hostile foreign bidder faces - depending on the drafting of the target's articles - either a difficult or impossible task. By simply denying approval, the target's management can always pass the buck to the bidder who then has to file court proceedings if it wants to succeed. This in itself is an impediment for a bidder. Although a bidder may theoretically to some extent circumvent the restricted transferability of the shares by entering into shareholder agreements with the holders,²⁷¹ this will often be difficult to be put into practice, especially by a foreign bidder.

However, outside the insurance sector, the chance that registered shares with restricted transferability will become widespread in listed stock corporations seems quite remote. To convert ordinary shares into registered shares would require a unanimous decision by the general meeting,²⁷² which is virtually impossible to achieve. Restricted shares may either be issued when a new company is floated or when an already existing company increases its capital. But in the present climate there is no indication that the issue of registered shares with restricted transferability is becoming increasingly popular. Given the huge structural barriers and the easier option of limited voting rights there is no need for this measure either. If hostile takeover bids were to increase drastically, this might change to a certain extent. However, as far as listed stock corporations are concerned, the provisions contained in the Listing

271 Otto, *Übernahmeversuche bei Aktiengesellschaften*, BB Beilage 12/88, p. 6; *Marquardt*, *Gesellschafts- und steuerrechtliche Instrumente zur Abwehr feindlicher Übernahmen von Aktiengesellschaften*, WiB 1994, 537, 538.

272 Sec. 180 II AktG.

Admission Rules would limit extensive listing of registered shares with restricted transferability.²⁷³

4.3.3. Cross Shareholdings

As far as mutually supportive holdings are concerned, circumstances in Germany seem not too different from those in Britain and reference is therefore made to Chapter 3.3.3.²⁷⁴ However, the rather insufficient disclosure provisions in Germany have rendered it difficult in the past to uncover the real extent of cross shareholdings which has been very strongly criticized.²⁷⁵ The newly introduced Securities Trading Act, the disclosure provisions of which entered into force in 1995, might bring some change with respect to *listed* stock corporations.²⁷⁶ At present it is estimated that about 70 to 75 per cent of all stock corporations in German belong to a corporate group.²⁷⁷

In Britain, mutually supportive stakes are to some extent restrained by the mandatory bid requirement in Rule 9 of the City Code, the relevant threshold of which is 30 per cent. In Germany, the Stock Corporations Act legislates against them, though it does so in a rather half-hearted way.²⁷⁸ The basic principle of the provision here concerned is that where two companies hold stakes of at least 25 per cent in each other the company which last passed the 25 per

273 Sec. 5 II Nr. 2 Börsenzulassungsverordnung.

274 See pp. 75.

275 Adams, Die Usurpation von Aktionärsbefugnissen mittels Ringverflechtung in der "Deutschland AG", AG 1994, 148; Göring, Die Verbreitung zwei- und mehrstufiger Unternehmensverbindungen, AG 1993, 538; *Emmerich/Sonnenschein*, Konzernrecht, § 1 III 2d.

276 See Chapter 4.1.2. at pp. 122.

277 *Emmerich/Sonnenschein*, Konzernrecht, § 1 III 2d. For an empirical study see Göring, Die Verbreitung zwei- und mehrstufiger Unternehmensverbindungen, AG 1993, 538, 543.

278 Sec. 328, 19 AktG (APPENDIX 2). For a detailed discussion of mutually supportive holdings in Germany see *Emmerich/Sonnenschein*, Konzernrecht, § 5.

cent threshold must - regardless of the size of its stake - not exercise voting rights exceeding 25 per cent, whereas the votes of the other company are not restricted. For example, where company A acquires 30 per cent in company B and B subsequently purchases 40 per cent of the shares in A, then B must not vote those shares exceeding the 25 per cent threshold.

Hence, large mutually supportive holdings remain legal. Since many of them are held for genuine investment reasons, it seems doubtful whether a further confinement would be economically justifiable. Admittedly, however, they may well be used as effective defences.²⁷⁹

4.4. Defences against an existing Offer

Before turning to the individual measures available to a defending management, the rather fundamental question has to be answered whether the management of a German stock corporation is generally empowered to take any defensive steps.

4.4.1. Admissibility of Defensive Actions

In Germany, the Stock Corporations Act does not deal specifically with this question. In principle, however, it is acknowledged that the management has to remain neutral with respect to the composition of the shareholders.²⁸⁰ This principle of

279 Adams, Die Usurpation von Aktionärsbefugnissen mittels Ringverflechtung in der "Deutschland AG", AG 1994, 148, 153.

280 Adams, Was spricht gegen eine unbehinderte Übertragbarkeit, AG 1990, 243, 246 f.; Assmann/Bozenhardt, in: Assmann/Basaldua/Bozenhardt/Peltzer, Übernahmeangebote, S. 113 f.; Ebenroth/Daum, Die Kompetenzen des Vorstands einer Aktiengesellschaft, DB 1991, 1105, 1158; Hahn, Die Regulierung von

neutrality is also reflected in the voluntary German Takeover Code 1995. Its Article 19 prohibits, like the City Code,²⁸¹ to “*take any measures which conflict with the interests of the holders of securities in accepting the offer.*”²⁸² However, as the management has to act in the best interests of the company,²⁸³ the question arises whether there might be occasions in which the best interests of the company entitle or even require the management of the target board to resort to defensive actions against a hostile bidder. Three different schools of thought have developed.

(1) First, there are those who argue that the management may not take any defensive measures after a bona fide offer has been communicated.²⁸⁴ They stress that the management must not exercise any influence regarding the composition of the company’s shareholders, that it ought to be the shareholders who choose the management and not the other way round, that the existing shareholders must not be deprived of the opportunity to decide upon the merits of the offer themselves. This point of view is very much in line with the firm stance taken by the City Code.

(2) Antagonistically, others maintain that the management may take all steps they think fit as long as they act in the best interests of the company, which may include frustrating actions against a takeover bid.²⁸⁵ Their main argument is that the interests of a

Übernahmeangeboten in der Europäischen Gemeinschaft, ZBB 1990, 10, 19; *Hopt*, Aktionärskreis und Vorstandsneutralität, ZGR 1993, 534, 548 ff.; *Immenga*, Vertragliche Vinkulierung von Aktien, AG 1992, 79, 81; *ders.*, in: Kreuzer (Hrsg.), Öffentliche Übernahmeangebote, 1992, S. 11, 28 ff.; *Rümker*, Übernahmeangebote, in: Festschr. Heinsius, 1991, S. 683, 688

281 General Principle 7 and Rule 21 City Code. See Chapter 3.1.1.(2)(d) at pp. 35 and Chapter 3.4. at pp. 85.

282 See Chapter 4.1.1.(3)(d) at pp. 116.

283 To the precise meaning of this see *Mertens*, Kölner Kommentar zum AktG, § 76 Rn. 16 et seq.

284 *Adams*, Was spricht gegen eine unbehinderte Übertragbarkeit, AG 1990, 243; *Assmann/Bozenhardt*, Übernahmeangebote, p. 101 et seq.

285 *Martens*, Der Einfluß von Vorstand und Aufsichtsrat auf die Kompetenzen und Struktur der Aktionäre, in Festschrift für Beusch, p. 529 et seq.; *Werner*, Probleme “feindlicher” Übernahmeangebote im Aktienrecht, p. 5 et seq.

company do not only comprise the present shareholders' interests, but equally the employees' interests as well as public interests. Accordingly, where the management arrives bona fide at the conclusion that the takeover is detrimental to some of these wider issues they are not only entitled, but obliged to fight the offer.

(3) A third school of thought, which probably represents the majority of the legal community, tries to reach a compromise by arguing that in principle the management may not resort to defensive actions, save in extremely exceptional circumstances.²⁸⁶ Examples given for those circumstances include the situation where the bidder has a criminal back-ground, like a Mafia-organisation, where it is a politically discredited state, where the bidder acts in clear breach of the law or where the financing of the bid is unsound.

4.4.2. Actual Defensive Measures

Since hostile takeover bids are almost non-existent in Germany, there is little to no practical experience with actual defensive actions. Some measures used in Britain, like lobbying shareholders²⁸⁷ or searching for a white knight,²⁸⁸ are doubtlessly possible in Germany too.²⁸⁹

Drastic measures like the issue of authorised capital to a friendly holder through the exclusion of pre-emption rights²⁹⁰ or the

286 *Mertens*, in *Kölner Kommentar zum AktG*, § 76 Rn. 26; *Hopt*, *Aktionärskreis und Vorstandsneutralität*, ZGR 1993, 534; *Immenga/Hellberg*, *Corporate Takeover through the Public Market*, p. 28.

287 See Chapter 3.4.1. at pp. 86.

288 See Chapter 3.4.4. at pp. 94.

289 *Hauschka/Roth*, *Übernahmeangebote und deren Abwehr im deutschen Recht*, AG 1988, 181, 193.

290 Sec. 203 AktG. *Hopt*, *Aktionärskreis und Vorstandsneutralität*, ZGR 1993, 534, 560; *Marquardt*, *Gesellschafts- und steuerrechtliche Instrumente zur Abwehr feindlicher Übernahmen*, WiB 1994, 537, 541; *Otto*, *Übernahmeversuche bei Aktiengesellschaften*, BB Beilage 12/1988, 1, 8 et seq.

acquisition of its own shares by the target company²⁹¹ are very restricted both by statute and case law which makes these ploys inoperable in a takeover situation.

Unlike the City Code, there is no rule in German law which prevents the management of a targeted stock corporation from entering into contracts "*otherwise than in the ordinary course of business*."²⁹² Hence, if hostile bids became more frequent in Germany, it is rather likely that creative company lawyers would try to devise different forms of contractual "*poison pills*". Moreover, court proceedings during the offer period are unlike the U.K. in no way restricted and it is, thus, predictable that, like in the U.S., court proceedings on all kinds of grounds, like a breach of securities regulations, could be used as a ploy to block or delay the bidder's plans. A few measures which might possibly be adopted by the defending management are outlined below.²⁹³

(1) "Crown Jewel" Defence

A defence line, known in the U.S. as "*crown jewel*" defence, where the company sells or disposes of material assets or plants to a third party to thwart the bidder's plans might be taken in Germany too. Shareholder consent for such a measure is only required where the management either sells the entire assets of the company (75 per cent majority)²⁹⁴ or where the most important part of the company is sold (simple majority).²⁹⁵

291 Sec. 71 et seq AktG; Otto, Übernahmeveruche bei Aktiengesellschaften, BB Beilage 12/1988, 1, 8.

292 Rule 21(e) City Code.

293 See also Hauschka/Roth, Übernahmeangebote und deren Abwehr im deutschen Recht, AG 1988, 181, 191 et seq.

294 Sec. 361 AktG.

295 BGH 83, 122 (Holzmüller).

(2) Corporate Acquisitions

Like selling assets, it would equally be possible for the target company to acquire assets. The entrenched management could, thus, acquire a third company in order to increase its size and thwart the takeover bid by triggering the intervention of the competition policy authorities under the relevant merger regulations.

(3) "Pac Man" Defence

Not very likely in Germany, but legally thinkable still, is a defence line, known in the U.S. as "pac man" defence, where the target company replies by making a counter-offer for the predator company.

4.5. Concluding Remarks

The analysis has shown that there are no legally binding rules specifically designed to govern takeovers. The newly introduced voluntary Takeover Code 1995 is lacking an effective enforcement mechanism and can therefore at present not be expected to be taken seriously. It is clearly not in the same category with the City Code.

Due to the absence of a binding regulation in respect of, for example, equal treatment of shareholders, fixed time limits for the offer period, or a mandatory bid requirement, a bidder enjoys considerably more freedom than it does in Britain - at the expense of small investors, though.

In addition to the comparatively underdeveloped stock market in Germany, there are, however, a number of structural barriers inherent in German company law and corporate culture which effectively prevent a market for corporate control and render German Stock Corporations rather unattractive to foreign bidders. Although these barriers are not specifically intended to prevent takeover bids and do not inhibit the acquisition of shares or the announcement of a bid itself, they impede and delay the integration of the newly acquired company profoundly. It has been demonstrated that the two-tier board structure and the 75 per cent majority mostly required render the replacement of the old management difficult. Far reaching employee representation on supervisory board level complicates matters further, and certainly makes large German stock corporations less attractive, especially to foreign bidders who are not used to this kind of complicated corporate governance structure. Appointment rights to the supervisory board granted to certain shareholders may, together with employee representation, render a German Stock Corporation impregnable. If, however, the bidder manages to win control of the supervisory board, the rather complex German law of groups imposes a number of obligations which complicate the integration of the German company into the bidders group. Hence, even without any specific defences designed to put off a potential bidder, German stock corporations are difficult prey, and a British bidder would be confronted with a number of corporate governance features inherent in German law with which it is not familiar.

Given these structural barriers it is not surprising that there has been little need for additional protective measures. However, a simple, but nonetheless relatively effective measure frequently installed is the restriction of voting rights. Bearing in mind the huge influence of the banks as depositaries it is difficult to see how an unwelcome foreign bidder could overcome these obstacles.

In a hostile bid situation the management of a German target company would not to the same extent as the directors of a British public company be prevented from taking frustrating actions. Given the extreme rarity of takeover bids in Germany, it still remains to be seen to which measures a target management would resort, how effective these would be, and how the courts would react.

To sum up, it can not be ruled out that a bidder with substantial financial strength, determination, time, and precise knowledge of the German legal and economic system and business culture might succeed with a hostile bid now and again, but it clearly seems at present out of the question that public takeover bids will in the foreseeable future become as easy and popular as they are in Britain.

Chapter 5

EUROPEAN DEVELOPMENTS

Considering a level playing field for takeovers vital to the Common Market and stressing the need for harmonisation in this area, the EC-Commission tries to tackle the issue by two means: First, there is the "*Proposal for a 13th Directive on Company Law concerning Takeover Bids*", the latest version of which has been proclaimed in February 1996 (APPENDIX 6).¹ The proposal basically undertakes to ensure equal treatment, adequate information, and the protection of minority shareholders through providing for a certain takeover procedure. However, apart from restricting the use of certain defensive tactics,² it does little in terms of removing structural barriers to takeovers. This is left to the proposal for a "*Fifth Directive on Company Law concerning the Structure of Public Limited Companies*".³

While there is activity regarding the Takeover Directive, as the newly released 1996 version shows, the proposed Fifth Directive remains blocked, mainly due to the politically controversial issue of employee participation in public companies. Therefore, the greater part of this chapter will be devoted to the newly proposed Takeover Directive.

1 February 7, 1996. EC Doc. 95/0341, COM (95) 655 final.

2 Article 8 lit. a. See Chapter 5.1.2.(4) at pp. 193.

3 Amendment O.J. 1991, C 7/4; amended O.J. 1991, C 321/9. Up to date version published in *Dine*, EC Company Law, A8. See Chapter 5.2. at pp. 198.

5.1. The Proposed 13th Directive

The first effort to create a European law of takeovers dates back well over two decades when *Professor Robert R Pennington* presented his "*Report on Takeover and other Bids*" in 1974 which he drew up on behalf of the EC Commission.⁴ With *Professor Pennington* being an English law professor, Britain having by far the highest number of takeover bids and the most developed securities markets in Europe, and the City Code by and large having already proven its virtue as an efficient regulatory framework, it seems quite natural that all European takeover proposals, of which four were proposed to date, have ever since been heavily influenced by the British model.⁵

Sparked by Professor Pennington's proposal in 1974 a few articles were published on this matter,⁶ but the discussion of the idea of a European Takeover Directive soon died down in the following years, the reason being an international slow-down of takeover activity and a lack of a need for harmonisation in the field of takeovers. As far as Britain was concerned, the City Code was already in force at home⁷ and euro-wide acquisitions were not as frequent as today. Hence the issue of a "level playing field" was not as pressing as it is these days. Regarding Germany, takeover bids as a technique of acquiring control of a company were virtually

4 EC Doc. XI/56/74-E. The Pennington Report presented a first draft of a Takeover Directive. See *Bradley*, Harmonising Takeover and Merger Regulations within the EEC, [1986] *Company Lawyer*, Vol. 7, No. 4, p. 131, 135. Also *Immenga/Hellberg*, Corporate Takeovers through the Public Market, p. 25.

5 *Dine*, The Proposal for a Thirteenth Directive on Takeover, [1991] *Company Lawyer*, Vol. 12, No. 5, p. 83; For a comparison with the City Code see *Kenyon-Slade/Andenas*, The Proposed Thirteenth Directive, p. 149; also *Sealy*, The Draft Thirteenth E.C. Directive on Takeovers, p. 135, 140.

6 For major contributions see *Behrens*, Rechtspolitische Grundsatzfragen zu einer Europäischen Regelung für Übernahmeangebote, ZGR 1975, 433; *Bess*, Eine europäische Regelung für Übernahmeangebote, AG 1976, 169.

7 See Chapter 3.1.1. at pp. 29.

unheard of at that time. Therefore, from a German point of view it is self-evident that there was no need for any harmonisation in the field of takeovers.

It was not until 1987, a time when takeover activity was on the increase again, that the EC-Commission came up with a new proposal for a Takeover Directive.⁸ Taking account of recommendations by the European Economic and Social Committee⁹ and the European Parliament,¹⁰ a further amendment followed in 1990.¹¹ The 1987, 1989, and 1990 proposals, with which the current 1996 proposal contrasts sharply, were basically structured in the same way providing for a detailed legal regulation of takeover bids the cornerstone being the requirement of a mandatory bid modelled after the City Code. However, these proposals were almost unanimously fiercely rejected throughout Europe - albeit for different reasons - which led in summer 1991 to a standstill of the negotiations on the takeover-law harmonisation. However, in its declaration presented at the Edinburgh Summit in December 1992 the EC-Commission indicated its intention to go ahead with the project and to revise the 1990 proposal once again. In order to assess the views of the member states before starting to redraft the proposed Directive, a questionnaire¹² was sent to the member states in July 1993, which - as an interesting example of "harmonisation in practice" - is contained in APPENDIX 5. The intention to present a new proposal was reconfirmed at the European Council in Essen (Germany) in December 1994. Taking into account the outcome of the questionnaire, the latest proposal was finally adopted in February 1996. Unlike the previous amendments, this latest draft is not just

8 EC Doc. XV/63/87-E. The intention to present a new proposal for Takeover Directive was previously made known in 1985 in the EC White Paper on the completion of the Internal Market 1992.

9 O.J. C 298, 27.11.1989, p. 56.

10 O.J. C 38, 19.2.1990, p. 41.

11 O.J. C 240, 26.09.1990, p. 7. Published in *Dine*, EC Company Law, A14.

12 To this step see *Bovis*, Developments at European Union level, [1994] Company Lawyer, Vol. 15, No. 7, p. 213.

another proposal introducing minor changes, but rather a new start of the so far ill-fated harmonisation attempts trying a different approach. Contrary to the previous proposals, the current proposal abandons the ambitious plan of a detailed and precise Takeover Directive and confines itself to what it calls a “framework” Directive consisting of “*certain principles and a limited number of general requirements*.”¹³ This new approach leaves the Member States with ample room for manoeuvre on implementation of the Directive. However, it remains to be seen whether this “framework approach” really is not only a new, but also a constructive way forward on harmonizing European takeover laws and not just the result of a political deadlock, a Directive of the lowest common denominator avoiding all controversial issues. In order to understand why this new approach was taken, it appears useful to briefly examine which the main stumbling blocks to takeover harmonisation have been in the past (5.1.1.). After considering this, the 1996 proposal will be discussed in detail (5.1.2.).

5.1.1. Why did the previous Proposals fail?

The answer to this question can not be given uniformly without having regard to the individual Member States. However, the British and Germans appear to represent the two main factions and it seems therefore justified in the context of this thesis to concentrate on these countries.

(1) British Objections

Given the fact that the previous proposals for a Takeover

Directive exhibited many of the same features as the City Code,¹⁴ like for example the mandatory bid requirement, it seems at first glance rather surprising that, apart from few exceptions,¹⁵ the proposals were so strongly rejected throughout the British legal profession.¹⁶ Apart from a number of more or less serious flaws and inconsistencies in the drafting,¹⁷ which could have been corrected, the reason for this outright repudiation in Britain was not so much the substance of the proposed rules itself, but the fact that the well functioning self-regulatory system with all its virtues, namely flexibility and relative freedom from judicial interference during the bidding process, was feared to be threatened.¹⁸ In a thorough analysis of this issue, which appears to reflect the majority opinion in Britain on the past proposals quite well, *Kenyon-Slade* and *Andenas* wrote:¹⁹

“the Directive ... threatens to undermine the existing United Kingdom scheme by sweeping away the self-regulatory ethos which is so fundamental to the application and operation of the City Code. Specifically,

14 For a detailed comparison of the Directive with the City Code see *Sealy*, The Draft 13th EC Directive on Takeovers, p. 135, 140 and *Kenyon-Slade/Andenas*, The Proposed Thirteenth Directive, p. 149-188.

15 *Jowell*, The Takeover Panel: Autonomy, Flexibility and Legality, [1991] P.L. 149 et seq. See also a statement of the Scottish Law Society reproduced in *Dine*, EC Company Law, para 14.60 et seq the main argument being that a statutory system might have more regard to employees' interests and the interests of the general public. It also appears that at least in the past the Labour Party had objections against the self-regulatory system, see *Calcutt*, The Work of the Takeover Panel, [1990] Company Lawyer, Vol. 11, No. 11, p. 203, 206.

16 For a summary of the criticism and a reproduction of a number of official statements see *Dine*, EC Company Law, para 14.48-14.67. See also the criticism by the chairman of the Panel: *David Calcutt*, The Work of the Takeover Panel, [1990] Company Lawyer, Vol. 11, No. 11, p. 203, 207 and the Panel's Director General, *William Staple* in Rothschild man to head Panel, *Financial Times*, January 8, 1994; *Kenyon-Slade/Andenas*, The Proposed Thirteenth Directive, p. 149, 155; *Sealy*, The Draft Thirteenth E.C. Directive on Takeovers, p. 135, 143.

17 For example, there is no provision concerning the price of a mandatory bid. It would, hence, be possible for the offeror to offer a ridiculously low price which would reduce the mandatory bid requirement to absurdity. As to this point see *Wouters*, Towards a Level Playing Field, [1993] CMLRev 267, 281.

18 See in detail Chapter 3.1.2 at pp. 36.

19 *Kenyon-Slade/Andenas*, The Proposed Thirteenth Directive, p. 149.

the proposed Directive threatens to introduce a statutory system of takeover regulation which is likely to be plagued by excessive bureaucracy, inflexibility, and constant tactical litigation that would imperil the entire regulatory agenda."

From the German perspective, where self-regulation is traditionally regarded with suspicion and not seen as a serious alternative to statutory regulation, the British worries have never been fully understood. As Lord Donaldson put it in *Datafin*: "*Self-regulation is an emotive term*"²⁰ - and Germans by and large do not appear share this emotion.²¹ However, since the British experiences with self-regulation in the field of takeover bids have overall been very positive, the scepticism towards any Brussels-imposed changes seems understandable.²²

(2) German Objections

The German objections focused mainly on the requirement of a mandatory bid. Besides, the need for a takeover statute has been questioned.

This last point is somewhat evident in a country with hardly any Anglo-style public takeover bids.²³ As has been examined in

20 R. v. Panel on Takeovers and Mergers, ex parte *Datafin Plc.* [1987] QB 815, 826.

21 As to recent developments regarding the voluntary German Takeover Code 1995 see Chapter 4.1.1. at pp. 107.

22 Warning that the British fears might be exaggerated: *Jowell*, The Takeover Panel: Autonomy, Flexibility and Legality, [1991] P.L. 149 et seq. See also the statement of the Scottish Law Society reproduced in *Dine*, EC Company Law, para 14.62.

23 For an empirical study see *Wymeersch*, Unternehmensführung in Westeuropa, AG 1995, 299, 307. Also *Krause*, Zur Gleichbehandlung der Aktionäre bei Übernahmeangeboten und Beteiligungserwerb WM 1996, 845; *Neye*, Der neue Übernahmekodex, ZIP 1995, 1464; *Thoma*, Der neue Übernahmekodex der Börsensachverständigenkommission, Osnabrück, Arbeitspapier 9/96, p. 4.

Chapter 4.2, a number of structural legal, economic, and cultural barriers impede takeover bid activity as it exists in the U.K. Although the proposed, but blocked Fifth Directive makes some efforts in terms of removing these barriers, as will be further discussed below,²⁴ it is debatable whether the EC has set its priorities right and done enough to remove these barriers.

The opposition against the requirement of a full mandatory bid for all outstanding shares when a certain threshold (one third) was exceeded was insurmountable in Germany²⁵ with only few dissenting opinions.²⁶ As has been pointed out earlier,²⁷ there is no specific takeover law in Germany and the acquirer enjoys, apart from some disclosure provisions, complete freedom.

(a) One line of argument against the mandatory bid often put forward in Germany is that the requirement of a mandatory bid would render the acquisition of control more expensive which would be detrimental to the securities markets. It is also feared that such a rule would lead to further concentration and more intensive forms of control since it would not be possible any longer to acquire stakes of just, say, 40 or 50 per cent. The consequence, it is argued, were increased problems under the relevant merger control and

24 Chapter 5.2. at pp. 198.

25 *Assmann/Bozenhard*; *Übernahmeangebote*, p. 37; *Baums*, *Übernahmeregeln in der Europäischen Gemeinschaft*, ZIP 1989, 1376; *Assmann*, *Verhaltensregeln für freiwillige öffentliche Übernahmeangebote*, AG 1995, 563; *Grunewald*, *Der geänderte Vorschlag einer 13. EG-Richtlinie betreffend Übernahmeangebote*, WM 1991, 1361, 1362; *Hahn*, *Die Regulierung von Übernahmen in der Europäischen Gemeinschaft*, ZBB 1990, 10, 17; *Hommelhoff/Kleindiek*, *Takeover Richtlinie und europäisches Konzernrecht*, AG 1990, 106; *Mertens*, *Förderung von, Schutz vor, Zwang zu Übernahmeangeboten*, AG 1990, 252; *Peltzer*, *Übernahmeangebote nach künftigem Europa-Recht*, p. 179, 191, 231; *Sandberger*, *Teilübernahmeangebote und Zwangsübernahmeangebote im Europäischen Takeover-Recht*, DZWIR 1993, 319, 321 et seq; *Werner*, *Probleme "feindlicher" Übernahmeangebote*, p. 5, 12.

26 *Adams*, *Was spricht gegen eine unbehinderte Überbarkeit*, AG 1990, 243; *Hahn*, *Die Regulierung von Übernahmen in der Europäischen Gemeinschaft*, ZBB 1990, 10; *Reul*, *Übernahmeangebote in der ökonomischen Analyse*, p. 11, 23.

27 See Chapter 4.1. at pp. 107.

competition laws.

Whether this is a realistic picture is somewhat difficult to say. The British example with its flourishing securities markets suggests that the economic problems caused by a compulsory bid rule should not be exaggerated.²⁸ It should also be taken into consideration that the existence of a mandatory bid rule might well boost investor confidence in the markets - as the highest standard of equality of treatment can be ensured this way - which could contribute to a more active equities market.²⁹ However, this correlation is often overlooked or at least not given much weight in Germany.

(b) A second line of argument centres around the dogmatic consequences of a mandatory bid rule in Germany. As stated previously, the German law of groups offers a complex and sophisticated set of rules designed to protect minority shareholders within a subsidiary company.³⁰ Hence, it is reasoned that there is no need for any further protection by way of a mandatory bid rule in Germany. Steps in this direction should according to this opinion in any case be left to the European harmonisation of the law of groups through the proposed 9th Directive.³¹ The idea that small investors should participate in any premiums paid in connection with the transfer of large stakes is not generally accepted in Germany.³² Equal treatment of all shareholders, it is suggested, may better be achieved by a pro-rata-rule as stipulated by the U.S. Williams Act.³³

28 In this direction also *Hopt*, *Übernahmeangebote im europäischen Recht*, p. 187, 202.

29 *Reul*, *Übernahmeangebote in der ökonomischen Analyse*, p. 11, 24.

30 See 4.2.5. at pp. 151 and Appendix 2.

31 To this proposal *Palmer's Company Law*, para 16.430.

32 See for example *Grunewald*, *Der geänderte Vorschlag einer 13. EG-Richtlinie betreffend Übernahmeangebote*, p. 1361, 1363; *Hommelhoff/Kleindiek*, *Takeover Richtlinie und europäisches Konzernrecht*, AG 1990, 106, 107; *Lutter*, *Die Treuepflicht des Aktionärs*, ZHR 153 (1989), 446, 462; *Lüttmann*, *Kontrolwechsel in Kapitalgesellschaften*, 1992, S. 180 f, 208 f; *Mertens*, AG 1990, 252, 257; *Sandberger*, DZWir 1993, 319, 323 f; critical also *Baums*, ZIP 1989, 1377, 1379.

33 For a comparison with the U.S. rules see *Wouters*, *Towards a Level Playing Field*, [1993] CMLRev 267, 282.

Considering these arguments, it has to be admitted that the existence of a law of groups changes the legal parameters and makes a direct comparison with the situation in Britain, where no such set of rules exists, difficult. Because of the law of groups, the need to avoid minorities in subsidiary companies through a full mandatory offer is reduced and the position of minority shareholders in subsidiary companies is because of the extra protection offered by the law of groups probably somewhat better in Germany - at least in theory. On the other hand, it is almost unanimously acknowledged in Germany that the law of groups often fails to achieve its protective goal, particularly when it comes to so called qualified de facto groups.³⁴ Besides, a mandatory bid rule would not mean that the law of groups had to be abandoned or changed. Since not all mandatory bids would lead to a 100 per cent majority, having a law of groups would still make sense. It is true, however, that the introduction of a mandatory bid rule would mean a very radical change of law in Germany for which the legal and business community is despite the voluntary Takeover Code 1995 not ready yet.³⁵ Unfamiliarity with such a rule certainly accounts for some of the opposition.³⁶

5.1.2. The 1996 Proposal

Taking account of the objections discussed above, the 1996 proposal tries to appease both the British and German sides not only by pursuing the new framework approach, but also by (a) allowing a non-legal implementation of the Directive through self-regulatory rules and (b) abolishing the requirement of a mandatory bid. Although the new proposal covers most of the field of the 1990

34 See Chapter 4.2.5.(2) at pp. 154.

35 As to the somewhat "ill-bred" mandatory bid rule in the new voluntary German Takeover Code see Chapter 4.1.1.(4) at pp. 116.

36 In this direction *Hopt*, *Übernahmeangebote im europäischen Recht*, p. 187, 209.

proposal, it is much more loosely drafted specifically referring to the principle of subsidiarity³⁷ *“laying down a framework consisting of certain common principles and a limited number of general requirements which Member States will be required to implement through more detailed rules according to their national systems and their cultural contexts.”*³⁸ An indication of this new framework approach is the volume of the new proposal which consists of only 12 rather concise articles as opposed to 24 lengthy articles in the previous version.

(1) Scope

The scope the new draft is defined in Article 1 by three criteria relating to (a) the nature of the provisions which are to be harmonized, (b) the “nationality” of the target company and (c) the relevant securities subject to the bid.

(a) The nature of the provisions to be harmonized - Implementation of a Directive through Self-regulation?

The co-ordination measures prescribed by the proposed Directive apply not only *“the laws, regulations and administrative provisions”* but also - and this is new - to *“other mechanism or arrangements of the Member States relating to takeover bids.”*³⁹ This wording is no coincidence. It is a concession to the British delegation which has been adamant about keeping the self-regulatory system

37 Article 3b (3) EC-Treaty: *“Any action by the Community shall not go beyond what is necessary to achieve the objectives of this Treaty.”*

38 Preamble, indent 7.

39 The phrase *“other mechanisms or arrangements”* is also used in Article 3 (1) and Article 11 (1).

as established under the City Code.⁴⁰ However, it is questionable whether the implementation of a Directive purely through self-regulatory rules without any legal backing is lawful under the EC-Treaty.

Article 189 (3) EC-Treaty stipulates: “A *Directive shall be binding, as to the result to be achieved, upon each Member State to which it is addressed, but shall leave to the national authorities the choice of form and methods.*” This article leaves no doubt that addressees of a Directive are Member States only.⁴¹ Only Member States can be held responsible by the EC-Commission through the treaty violation proceedings under Article 169 EC-Treaty. Hence, if a private body were to implement a Directive there would be no way for the EC-Commission to take any action against it in case of non- or inadequate implementation which would contradict the enforcement system set up by the EC-Treaty. Moreover, according to Article 189 (3) it is the “*national authorities*” who are charged with implementing Directives. The term “*national authority*”, however, implies the body charged with this duty has to have some legal backing. With respect to the British legal system it could perhaps be argued, as *Lord Donaldson* in effect did in the *Datafin* case concerning judicial review proceedings against the *private* Takeover Panel,⁴² that under certain circumstances a private institution performing public duties can be deemed to be a public body, or in other words a *national authority*. Yet, from a European perspective, the question is not only how individual member states define the term “*national authority*”, but whether there are under European law certain qualifications which are to be met by a “private institution” in

40 The phrase in question was inserted virtually at the last minute giving way to British pressure. As to the political background see Neye, Der neue Vorschlag der Kommission für eine dreizehnte Richtlinie über Übernahmeangebote DB 1996, 1121, who is high-ranking official in the German Ministry of Justice and was involved in the negotiations.

41 See also Article 12.

42 R. v. Panel on Takeovers and Mergers, ex parte Datafin Plc. [1987] QB 815, 838. As to details see Chapter 3.1.2.(4) at pp. 51.

order to qualify as a “*national authority*” within the meaning of Article 189 (3) EC-Treaty. Although the ECJ repeatedly stated that a Directive is “*binding on all the authorities of Member States including, for matters within their jurisdiction, the courts*”⁴³ there is no decision specifying what is required for an institution to be considered a “*national authority*”. Hence, whether the Takeover Panel having no statutory, prerogative or common law powers would be considered a “*national authority*” by the ECJ is at least doubtful.⁴⁴ However, an argument in favour of recognition of the Panel as “*national authority*” is that it is - in theory, not necessarily in practice - subject to judicial review.

However, even if the Panel were considered a “*national authority*” there is one more problem connected with the idea of implementation through self-regulation. The ECJ has long established that Directives have to be implemented by *binding* acts, and that can only mean that there has to be some legal backing. In a case against Belgium the ECJ stated in no uncertain terms: “*It should be remembered, in that regard, that according to the consistent case-law of the Court, each Member State must implement Directives in a manner which fully meets the requirement of legal certainty and must consequently transpose their terms into national law as binding provisions.*”⁴⁵ A purely self-regulatory system would not meet these requirements.⁴⁶ Unlike legislation in whichever

43 Von Colson and Kamann v. Land Nordrhein-Westfalen (Case 14/83), [1984] ECR 1891, 1909, para 26; Marguerite Johnston v. Chief Constable of the Royal Ulster Constabulary (Case 222/84), [1986] 1651, 1690, para 53.

44 As to the Panel’s status see R. v. Panel on Takeovers and Mergers, ex parte Datafin Plc. [1987] QB 815, 825. Also Chapter 3.1.2.

45 Commission of the European Communities v. Kingdom of Belgium (Case 239/85), [1986] 3645, 3659, para 7. See also the similar wording in Commission of the European Communities v. Federal Republic of Germany (Case 361/88), [1991] 2567, 2600, para 15.

46 See also Commission of the European Communities v. Federal Republic of Germany (Case 361/88), [1991] 2567, 2600, para 15: “*It should be borne in mind in that respect that, according to the case-law of the Court, the transposition of a directive into domestic law does not necessarily require that its provisions be incorporated formally and verbatim in express, specific legislation; a general legal context may, depending on*

form, self-regulatory rules, however well enforced, do ultimately not have the force of law.⁴⁷ This is acknowledged by the City Code itself which states in the introduction: “*The Code has not, and does not seek to have, the force of law.*”⁴⁸ In terms of European policy, the objective of harmonizing the *laws* of the Members States, and that is what Directives are about, would be compromised if Members States were allowed to leave the implementation of Directives to ultimately non-accountable private bodies. If a self-regulatory approach toward takeover regulation were wanted, the given instrument on European level would be the *Recommendation* under Article 189 (4) EC-Treaty which does not have the force of law.⁴⁹ A Directive, however, requires *legal* implementation. Although conceding that the City Code “*resembles legislation*”⁵⁰ and is recognized by the courts,⁵¹ the government and other regulatory authorities in Britain,⁵² for the reason given above it is submitted that under European law the City Code could not pass as a proper implementation of the proposed Directive unless it has some statutory backing. A legislative “framework” act would be required under Article 189 (3) EC-Treaty. The proposed Directive in effectively allowing implementation through self-regulatory “*mechanisms or arrangements*” consequently infringes primary EC-law, namely Article 189 (3) EC-Treaty. A

the content of the directive, be adequate for the purpose, provided that it does indeed guarantee the full application of the directive in a sufficiently clear and precise manner so that, where the directive is intended to create rights for individuals, the persons concerned can ascertain the full extent of their rights and, where appropriate, rely on them before the national courts.” Also *Commission v. Netherlands* (Case 160/82), [1984] CMLR 1 230; *Commission v. Netherlands* (Case 291/84), [1989] 1 CMLR 479. To the nature of directives *Lasok*, *European Law*, p. 122.

47 For analysis of the phenomenon of self-regulation see *Page*, *Self-Regulation: The Constitutional Dimension*, (1986) 49 MLR 141-167.

48 City Code, Introduction, para 1(c).

49 For details see *Lasok*, *European Law*, p. 135.

50 These words were used by *Watkins L.J.* in *R. v. Spens* [1991] 1 W.L.R. 624, 632 (C.A.).

51 *R. v. Panel on Takeovers and Mergers, ex parte Datafin Plc.* [1987] QB 815; *R. v. Panel on Takeovers and Mergers, ex parte Guinness Plc.* [1989] 1 All ER 509; *R. v. Spens* [1991] 1 W.L.R. 624 (C.A.)

52 As to the enforcement of the City Code see Chapter 3.1.2.(3) at pp. 44 and (4) at pp. 51.

Member State relying on a functioning self-regulatory system instead of transposing the Directive into its *legal* system would - for technical reasons - act in breach of Article 189 (3) of the EC-Treaty even if the self-regulatory rules would meet - as the City Code does - all the substantive requirements of the Directive. Hence, the words “*other mechanisms or arrangements*” should be deleted in Article 1 of the new proposal which would mean a return to the wording of the 1990 proposal.

(b) Offeree Company governed by the Law of a Member State

A further pre-condition to the applicability of the new proposal is that the offeree company⁵³ is “*governed by the law of a Member State*”. The criteria necessary to determine by which law a company is governed are not specified in the proposal. This silence can be interpreted in two ways. (1) First, one could argue that the question of whether a company is governed by the law of a Member State should - as a conflict of laws question - be left to the individual Member States. However, this could lead to conflicting results as different connecting factors are favoured by the Member States. In English law, a corporation is domiciled in the country in which it was incorporated, while most European countries including Germany connect a corporation to the country in which it has its actual headquarters.⁵⁴ Hence, a company headquartered in England but having been established under, say, Czech law would from an English standpoint considered a Czech company, to which the Directive would not be applicable. This would not necessarily be the

53 Defined in Article 2 as the “*company whose securities are the subject of the bid.*”

54 Stone, *The Conflict of Laws*, p. 106; *Ebenroth*, in *MünchKommBGB*, nach Article 10 EGBGB, para 139 et seq.

case from a German standpoint. (2) Those divergencies could be avoided if the question of which law governs a company would - at least in the context of interpreting a European Directive - be answered uniformly. The route to such a uniform European conflict-rule is shown in Article 58 (1) of the EC-Treaty. Under this provision only "*companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Community*" enjoy the right of establishment. If these criteria were applied in the present context to determine whether a company is governed by the law of a Member State, discrepancies with respect to the scope of the Directive could be avoided.⁵⁵

(c) Securities admitted to trading on a Stock Exchange

As a third pre-condition, the proposed Directive applies only to those companies governed by the law of a Member State whose securities are admitted to trading wholly or partially on one or more Stock Exchanges in the Community. Securities are defined as transferable securities carrying voting rights in a company or conferring entitlement to obtain transferable securities carrying such rights.⁵⁶

The limitation of the proposed takeover rules to target companies whose shares are admitted to trading on a Stock Exchange indicates that the Directive is placed in the field of capital market law rather than company law. The approach contrasts with the original 1989 proposal⁵⁷ and with the City Code,⁵⁸ both of which

55 As to the idea of Article 58 (1) EC-Treaty as a uniform European conflict-rule see *Ebenroth*, in *MünchKommBGB*, nach Article 10 EGBGB, para 196.

56 Article 2.

57 Article 1 Proposal 1989.

58 City Code, Introduction, para 4 (a).

apply to listed and unlisted public companies, but is in line with the 1990 proposal⁵⁹ and the German Takeover Code.⁶⁰ The approach taken by the 1989 proposal and the City Code seems preferable, though. If there is a need for a harmonization of takeover laws and if it is considered necessary to provide for extra protection of minority shareholders during a bid, it is difficult to see why only shareholders of listed companies should enjoy these rights. One could even argue that shareholders of non-listed public companies need the additional protection even more as for them selling their stocks may in the absence of a regulated market and the protection of the Stock Exchange not be as easy as for shareholders of listed companies. Therefore, a return to the wording of the original 1989 proposal seems desirable.

(2) General Principles

Clearly influenced by the City Code, the new proposal contains in addition to a number of more specific rules five General Principles.⁶¹ These General Principles are in harmony with those of the City Code⁶² and the voluntary German Takeover Code⁶³ (equality, sufficient information, transparency in dealings, restriction on defensive action). Also in line with the City Code and the German Takeover Code, the supervisory authority may, on the basis of a reasoned decision - quite like the British Takeover Panel⁶⁴ and the German Takeover Commission⁶⁵ - modify or relax the rules if it considers this appropriate in the individual case as long as it adheres

59 Article 1 Proposal 1990.

60 German Takeover Code, Definitions "*Target*".

61 Article 5.

62 See Chapter 3.1.1.(2) at pp. 32.

63 See Chapter 4.1.1.(3) at pp. 112.

64 City Code, Introduction, para 3 (a).

65 See Chapter 4.1.1.(5)(a) at pp. 119.

to the underlying purpose of the General Principles⁶⁶ which read as follows:⁶⁷

- (a) *all holders of securities of an offeree company who are in the same position are to be treated equally;*
- (b) *the addressees of a bid are to have sufficient time and information to enable them to reach a properly informed decision on the bid;*
- (c) *The board of an offeree company is to act in the interests of the company as a whole;*
- (d) *false markets must not be created in the securities of the offeree company, of the offeror company, or of any other company concerned by the bid;*
- (e) *offeree companies must not be hindered in the conduct of their affairs for longer than is reasonable by a bid for their securities.*

(3) Protection of Minority Shareholders

The protection of minority shareholders when a change of corporate control takes place has always been *the* central issue in the takeover harmonisation attempts. The previous proposal, influenced by the City Code, provided for a mandatory bid to all target shareholders giving them the right not only to leave the target company, but also to participate to some extent in the control premiums paid. As has been pointed out earlier, the majority opinion in Germany - and other continental countries⁶⁸ - does not (yet) accept the wisdom of a mandatory bid rule, but believes in the concept of protecting minority shareholders through a particular set of rules, namely the law of groups, designed to protect minority

66 Article 4 (4).

67 Article 5 (a) corresponds with Principle 1 of the City Code;
 Article 5 (b) corresponds with Principle 4 of the City Code;
 Article 5 (c) corresponds with Principles 7 and 9 of the City Code;
 Article 5 (d) corresponds with Principle 6 of the City Code;
 only Article 5 (e) has no direct equivalent among the City Code's principles, but the content of this principle is an overriding value of the City Code as well.

68 For the Netherlands see *Wymeersch*, *The Mandatory Bid: A Critical View*, in *Hopt* (ed.), *European Takeover Regulation*, 1992, p. 351 et seq.

shareholders in subsidiaries once a control-relationship has been established. As the disparity of views has proved insurmountable, the EC-Commission capitulated on this point which is the single most significant change of the new proposal. The new proposal only requires that following the acquisition of “*control*” national rules give proper safeguards to minority shareholders. However, the proposal leaves it for the Member States to either provide for a mandatory bid rule (for which case the proposal contains some provisions in Article 10) or to provide for “*other appropriate and at least equivalent means in order to protect the minority shareholders*” of the target company. The Explanatory Memorandum to the new proposal more specifically points to the law of groups as it exists in some continental Member States.

Article 3 Protection of minority shareholders

(1) Where a natural person or legal entity who as a result of acquisition, holds securities which added to any existing holdings give him a specified percentage of voting rights in a company referred to in Article 1, conferring on him the control of that company, Member States should ensure that rules or other mechanisms or arrangements are in force which either oblige this person to make a bid in accordance with article 10 or offer other appropriate and at least equivalent means in order to protect the minority shareholders of that company.

(2) The percentage of voting rights which confers control for the purposes of paragraph 1 and the way of its calculation shall be determined by the law of the Member State where the supervisory authority is located.

Article 3 in its present form provokes criticism for three reasons. First, there is the fact that Article 3 - like Article 1 - allows harmonisation through “*other mechanism or arrangements*”, i.e.

through self-regulation. As has been explained,⁶⁹ this amounts to a contravention of Article 189 (3) of the EC-Treaty which demands *legal* implementation. Secondly, the notion of *control* as drawn up in the new proposal appears problematic. Finally, the concept of “*other appropriate and at least equivalent means in order to protect the minority shareholders*” also engenders questions.

(a) Acquisition of Control

Contrary to the City Code,⁷⁰ the German Takeover Code,⁷¹ and the previous proposals,⁷² the newly proposed Directive refrains from defining the term *control*. Rather, it contains in Article 3 (2) a conflict rule according to which “*the percentage of voting rights which confers control ... and the way of its calculation*” is to be “*determined by the law of the Member State where the supervisory authority is located.*” Article 4 (2) stipulates that “*the authority competent for supervising the bid shall be that of the Member State in which the offeree company has its registered office if the securities of the company are admitted to trading on a regulated market in that Member State.*” Although this conflict-rule taken individually makes sense, the point is whether it is prudent as a matter of policy to abstain from introducing clear thresholds and calculation rules as for example contained in the City Code. The way the proposed Directive is drafted now, the whole affair is left to the individual Member States. Hence, Member States could define control as holding a 30, 50 or maybe 75 per cent stake of voting rights. Equally far-reaching could be the differences between the rules governing the calculation

69 Chapter 5.1.2.(1)(a) at pp. 181.

70 Rule 9.1. City Code: 30 per cent. See Chapter 3.1.1.(2)(a) at pp. 32.

71 Article 16 German Takeover Code: 50 per cent. See Chapter 4.1.1.(4) at pp. 116.

72 Article 4 (1) Proposal 1989 and 1990: the percentage could be defined by the Member State but was not to exceed one third of the voting rights.

of holdings (who is acting in concert etc.). The harmonizing effect of this rule is zero. Given that the protection of minority shareholders is considered a central issue by the EC-Commission, some common threshold which triggers the application of the minority protection rules and some common principles as to the calculation of holdings seem indispensable if a harmonized protection of minority shareholders is really wanted.

(b) Mandatory Bids

As has been explained, the mandatory bid is no longer treated as the only means to protect minority shareholders. However, where Member States opt for a mandatory bid rule, Article 10 which contains some minimum requirements applies. The new proposal permits both full and partial bids. In both cases, the offer has to be made to *all* shareholders which follows as a matter of course from the principle of equal treatment of shareholders. A partial bid has to be made for a “*substantial part*” of the remaining shares. According to the Explanatory Memorandum of the proposed Directive this “*percentage should be high enough to meet the objective of the protection of minorities.*” There is, however, no hint as to how much precisely that would be. Shares tendered in excess of what the offeror of the partial bid is willing to acquire have to be scaled down in the same proportion with respect to each shareholder (scaling down pro rata). This rule ensures equal treatment and corresponds with the relevant provision on partial bids of the City Code⁷³ and the German Takeover Code.⁷⁴

A serious shortcoming of Article 10 is that it is rather vague on the price of a mandatory bid. Unlike the City Code under which the

73 Rule 36.7 City Code.

74 Article 10 German Takeover Code.

bidder has to offer the highest price paid for shares of the target company within a specified period of time to enable all shareholders to participate in premiums paid, Article 10 of the new proposal only provides that the offer should be made “*at a price which meets the objective of protecting*” the shareholders’ interests. Again, the proposal is vague on a crucial matter. Thus, Member States could try to dilute the mandatory bid rule by allowing a mandatory bid price significantly below the premium (as the German Takeover Code effectively does).⁷⁵

(c) Other appropriate Means

In addition to the mandatory bid, Article 3 of the new proposal now allows “*other appropriate and at least equivalent means in order to protect the minority shareholders.*” The Explanatory Memorandum to the 1996 proposal points out that this new approach was necessary to accommodate certain Member States (Germany most notably) which protect minorities through a law of groups. In practice, it will be most difficult for the EC-Commission and the ECJ to assess whether the law of groups or other mechanism of a Member State really is equivalent to a mandatory bid in all respects. The scenario of the EC-Commission taking action against Germany before the ECJ under Article 169 of the EC-Treaty because the German law of groups provides for insufficient protection in the case of qualified de facto groups seems hardly realistic. Article 3 clearly is the result of a political compromise the intention of which was to enable the Member States to keep their national rules.⁷⁶ Again, the harmonizing effect of this rule, if there is any, is minimal.

⁷⁵ See Chapter 4.1.1.(4) at pp. 116.

⁷⁶ As to the political background see Neye, Der neue Vorschlag der Kommission für eine dreizehnte Richtlinie über Übernahmeangebote DB 1996, 1121.

The regulatory minimalism exercised by the EC-Commission begs the question whether a harmonisation at such a low level still makes sense. Article 3 demonstrates that a real consensus on the protection of minority shareholders in the context of a change of control of a company is not achievable at present. Article 3 not even defines the notion of control let alone the way in which minority shareholders are to be protected. As long as time is not ripe for a European solution on the protection of minority shareholders, which is obviously the case at present, it is submitted that the issue should be excluded from the proposed takeover Directive. The regulation of takeover bids would still make sense without provisions on the protection of minority shareholders. In fact, the issue of protection of minority shareholders goes far beyond the regulation of takeover bids anyway as public bids are just one technique to acquire corporate control. The protection of minority shareholders is a concern at the heart of company law independent from the acquisition technique applied. Hence, a takeover Directive should concentrate on regulating those (mainly procedural) issues specific to takeover bids (offer document, timing, duties of offeror and offeree company, supervisory authority etc.) and leave the more general issue of minority protection to a possible later Directive - if and when real consensus is reached among the Member States.

(4) Restrictions on Defensive Action

In line with the City Code,⁷⁷ the German Takeover Code,⁷⁸ and the previous proposals,⁷⁹ the management of the target company is obliged to refrain from adopting defensive measures which may

77 Rule 21 City Code. See Chapter 3.1.1.(2)(d) at pp. 35.

78 Article 19 German Takeover Code. See Chapter 4.1.1.(3)(d) at pp. 116.

79 Article 8 Proposal 1989 and 1990.

result in the frustration of the bid.⁸⁰ However, this rule takes effect only once the announcement of the intention to make a bid is made by the offeror. Prior to this point of time, the general company law rules of the individual Member States apply.

As to court proceedings as a defensive measure, it is left to the Member States to determine to what extent the courts may intervene in a takeover bid as long as an injured party enjoys “*adequate remedies, whether through an appeals procedure operated by the supervisory authority or through the right to take proceedings before the courts to claim compensation.*”⁸¹

(5) Procedural Rules

As a consequence of the framework-approach pursued by the 1996 proposal, the procedural provisions are reduced to an absolute minimum. A feature known from the City Code is that a high standard of transparency is sought to avoid insider-trading in advance of a bid. Therefore, Article 6 requires that “*the decision to make a bid is made public*” and that the supervisory authority and the management of the target company are informed previously by the bidder. Article 6 (3) provides for a basic minimum content of the offer document which is to be made public. The way the offer document and other relevant information is to be made public is left to the Member States. Member States only have to ensure that the creation of false markets in the securities of the offeree and offeror companies are avoided and that the relevant information is readily and promptly made available to the addressees of the bid.⁸² The offer period may not be less than four or more than ten weeks. The management of the target company has to publicise “*a document setting out its*

80 Article 8 lit (a).

81 Article 4 (5).

82 Article 7.

opinion on the bid together with the reasons on which it is based."⁸³ Contrary to the City Code, there is no obligation on the target management to seek and publish "*competent independent advice.*"⁸⁴ Unlike the previous proposals, the 1996 version contains no provisions on the withdrawal or nullity of the bid, the revision of bids, competing bids, or the disclosure of the result of bids. It simply states in Article 9 that the Member States have to ensure that rules are in force which govern at least these issues. Thus, as has been repeatedly pointed out in other contexts, the harmonizing effect with regard to procedural rules is minimal indeed. The City Code would easily fulfill all the procedural requirements.

(6) Supervisory Authority

As the previous proposals,⁸⁵ the draft Directive provides for a supervisory authority which is to be charged with supervising all aspects of the bid. Contrary to the previous proposals according to which the designated (state) authority could delegate all or part of its powers to "*associations or private bodies*", the new proposal allows the direct designation of "*associations or private bodies*" without prior delegation from a (state) authority. The supervisory authorities must have "*all the powers necessary for the exercise of their functions, which shall include responsibility for ensuring that the parties to a bid comply with the rules made pursuant to the Directive.*" Notwithstanding the high level of enforcement achieved by the British Takeover Panel through the co-operation with other (statutory) bodies like the Stock Exchange and the SIB,⁸⁶ it is difficult to see how a private body with no legal backing should be able to properly

83 Article 8 lit (a).

84 Rule 3.1 City Code.

85 Article 6 Proposal 1989 and 1990.

86 See in detail Chapter 3.1.2.(3)(d) and (e) at pp. 46 and 48.

enforce the proposed rules in every case. Again, the question arises whether the self-regulatory approach allowed by this proposal is in line with primary EC law, namely Article 189 (3) of the EC-Treaty.⁸⁷

(7) Summary

As the proposed Directive only undertakes to create “a *framework consisting of certain principles and a limited number of general requirements*” concerning takeovers one could not expect detailed regulation covering all aspects of a topic as complex as takeover bids. Though acknowledging that the principle of subsidiarity should play a major role in future harmonisation efforts, it appears doubtful in the case of the proposed Takeover Directive whether a harmonisation at such a low level would still make sense. Apart from the issue of defensive measures the proposed Directive backs down from all controversial issues. This is most manifest with respect to the protection of minority shareholders in the context of a change of control. Furthermore, to allow harmonisation by way of self-regulation, as the proposal does, may accommodate British objections, but is - to say the least - highly problematical with respect to primary European law. The procedural rules are so loosely drafted that the harmonizing effect would be minimal. The contribution of the proposed Directive towards a “level playing field” for takeovers and mergers would therefore be minuscule. Time simply appears not to be ripe for a substantive harmonisation of takeover laws. Under these circumstances it seems more in line with the principle of subsidiarity to just shelve the proposal until a substantive consensus is reached than to adopt a fragmentary and problematic Directive which is neither fish, flesh, nor fowl.

In the U.K. the new proposal has already provoked strong

87 See Chapter 5.1.2.(1)(a) at pp. 181.

opposition from the Takeover Panel,⁸⁸ for whom any Takeover Directive would mean a loss of power and more accountability, the Law Society and the House of Lords Select Committee.⁸⁹ The greatest British concern appears to be, as in the past,⁹⁰ that the directive would undermine the Takeover Panel and the City Code by making the regulatory system in the U.K. statutory. *Mr Alistair Defriez*, the Panel's director general (1996), is quoted as saying that "*tactical or nuisance litigation would inevitably result*" and that the Directive might lead compensation claims of up to £1 billion from losing bid battles.⁹¹ The 1995-1996 Report of the Takeover Panel reads as follows:⁹²

"The Panel does not believe that there would be any benefit for takeover regulation in the UK if these proposals were adopted and, indeed, it is concerned about the risks which they would pose to the existing system. In particular, the Directive, which would require statutory implementation, could lead to a legalistic interpretation of the Code with the consequent risk of greater resort to and intervention by the Courts. Participants in takeovers would inevitably seek to challenge Panel decisions which might lead not only to the granting of injunctive relief by the Courts in the UK but also to issues being referred to the European Court of Justice. It could result in tactical litigation between the parties. This interference with the takeover process would adversely affect the speed, flexibility and certainty with which the Panel is currently able to operate and would add significantly to the costs and disruption incurred during the course of a bid.

The Panel continues to question both the need for this Directive as most Member States have in recent years introduced measures to regulate takeovers and the need for action on a European basis under

88 Takeover Panel, 1995-1996 Report, p. 12

89 See *Financial Times*, 2 August 1996. Welcoming the proposal in principle as "a first step" and rejecting the claim that it would lead to tactical litigation, *Andenas*, European take-over regulation and the City Code, [1996] *Company Lawyer*, Vol. 17, No. 5, p. 150, 152: "There is no reason to fear that a takeover directive will lead to more litigation and undermine the City Code and the Takeover Panel. The English case law is clear in this respect, and the European Commission's 1996 proposal contains provisions making it possible to exclude new remedies."

90 See Chapter 5.1.1.(1) at pp. 175.

91 See *Financial Times*, 20 June 1996.

92 At p. 12.

the principle of subsidiarity."

The German industry, in contrast, has generally welcomed the new proposal⁹³ the underlying reason for this positive reaction probably being that a Directive as proposed would have very little if any practical effect and would, hence, be without serious consequences for the cherished German system.

5.2. The Proposed 5th Directive

The first version of this Directive was proposed in 1972 and has since repeatedly been amended,⁹⁴ the latest amendment being made in 1991.⁹⁵ The proposed Directive deals with a number of important issues, namely the structure of the management of a public company, employee participation, directors' liability and voting rights. The fundamental obstacle to agreement from the British point of view has always been the highly political question of employee participation.⁹⁶ Quite apart from this rather overshadowing issue,⁹⁷ the proposal in its latest version contains a number of provisions

93 *Gemeinsamer Arbeitsausschuß des Bundesverbandes der Deutschen Industrie, des Bundesverbandes Deutscher Banken, der Bundesvereinigung der Deutschen Arbeitgeberverbände, des Deutschen Industrie- und Handelstages, des Gesamtverbandes der Deutschen Versicherungswirtschaft für Fragen des Unternehmensrechts, Stellungnahme zum Vorschlag für eine 13. gesellschaftsrechtliche Richtlinie über Übernahmeangebote, RV 47/86 of 29 March 1996. Also Baums, The New Draft Proposal for a Directive on Takeovers - the German Perspective, Osnabrück, Arbeitspapier 10/96.*

94 As to its history see *Palmer's Company Law*, para 16.402.

95 [1991] O.J. C321/9. Up to date version published in *Dine*, EC Company Law, A8.

96 See e.g. *Boyle*, Draft Fifth Directive: Implications for Directors' Duties, Board Structure and Employee Participation, [1992] *Company Lawyer*, Vol. 13, No. 1, p. 6 at p. 8; *Hopt*, Labour Representation on Corporate Boards: Impacts and Problems for Corporate Governance and Economic Integration in Europe, *International Review of Law and Economics*, (1994) 14, 203-214.

97 *Palmer's Company Law*, para 16.402.

designed to remove some of the existing barriers to takeovers.⁹⁸

5.2.1. Removal of Directors

It has been seen that removing the incumbent management from office is one of the main difficulties encountered by a bidder for a German stock corporation.⁹⁹ In order to remedy this barrier, Article 36 (3) of the proposed Directive provides that *“for resolutions appointing or dismissing members of the administrative, management or supervisory organ, neither the law nor the memorandum or articles of association may require a majority greater than the absolute majority of votes”*

Being in line with section 303 (1) of the British Companies Act 1985, this provision would affect section 108 of the German Stock Corporations Act according to which, if no other provision is contained in the articles, a three-quarter majority is needed to appoint and remove those members of the supervisory board who are shareholder representatives.¹⁰⁰ Moreover, the law regarding special appointment rights in Germany would be affected.¹⁰¹ As discussed earlier, special rights to appoint up to one-third¹⁰² of the shareholder representatives of the supervisory board may be granted to certain shareholders and only those shareholders are at present entitled to remove the directors so appointed.¹⁰³ If

98 See Andenas, The future of EC company law harmonisation, [1994] Company Lawyer, Vol. 15, No. 4, p. 121; Dine, EC Company Law, A8.52 and A15.1 et seq.; Palmer's Company Law, para 16.448.

99 See Chapter 4.2.2. at pp. 133.

100 See Chapter 4.2.2.(2)(a) at pp. 137.

101 Sec. 101, 103 AktG. See Chapter 4.2.2.(2)(c) at pp. 141.

102 As to a restriction of the number of appointment rights see Articles 4 (5) and 21B (5) of the proposed 5th Directive: *“The memorandum or articles of association may not confer on the holders of a particular category of shares an exclusive right to put forward nominations for a majority of those members of the supervisory organ whose appointment is a matter for the general meeting.”*

103 Sec. 103(2) AktG.

Article 36 (3) were implemented, those specially appointed directors could - as any other shareholder representatives on the supervisory board - also be dismissed by an ordinary resolution of the general meeting which in turn would reduce the impeding effect of special appointment rights in Germany considerably.

Hence, the implementation of Article 36 (3) would render the supervisory board more accountable to the general meeting and, thus, facilitate the seizing of control over the corporate management organs by a successful bidder at the post acquisition stage. This is to be fully welcomed as a step in the right direction. It is to be expected, however, that the legally binding implementation of such a provision in Germany would be strongly opposed by many.

5.2.2. Restrictions on Voting Rights

Another major obstacle in Germany identified previously is the frequent restriction on the number of voting rights exercisable by a single shareholder.¹⁰⁴ Promoting the principle of "one share - one vote", Article 33 of the proposed 5th Directive in its latest version¹⁰⁵ would not only restrict the use of preference shares further, but also prohibit the limitation of voting rights in the way described.¹⁰⁶

In order to open the German market for corporate control and

104 See Chapter 4.3.1. at pp. 157.

105 Article 33: "(1) *The shareholder's right to vote shall be proportionate to the fraction of the subscribed capital which the shares represent.*
(2) *Notwithstanding paragraph 1, the laws of the Member States may authorise the memorandum and the articles of association to allow restriction or exclusion of the right to vote in respect of shares which carry special pecuniary advantages. Such shares may not be issued for an amount exceeding 50 % of the subscribed capital. Where the company has not fulfilled the obligations arising in respect of such shares for a period which may not exceed three consecutive accounting years, the holders of those shares shall acquire voting rights in proportion to the fraction of the subscribed capital which those shares represent, and the voting rights thus acquired shall be equivalent to those of the other shareholders.*"

106 *Palmer's Company Law*, para 16.449.

boost the equities markets by ensuring more shareholder-democracy while reducing the power of the banks, the new Article 33 is to be highly welcomed too. Again, however, many will take a different view in Germany.¹⁰⁷

5.2.3. Proxy Voting

Proxy votes, in Britain often exercised by directors¹⁰⁸ and in Germany by banks,¹⁰⁹ have been identified as barriers to takeovers in both countries, the problem being worse in Germany because of the additional influence of the banks through their holdings, their frequent representation on supervisory board level and the limitation of voting rights. Recognizing this problem, Article 28 restricts the freedom of the proxy to vote the shares to some extent.¹¹⁰ In

107 See e.g. Zöller/Noack, One share - one vote? AG 1991, 117, 128.

108 See Chapter 3.3.2. at pp. 74.

109 See Chapter 4.2.3. at pp. 143.

110 Article 28: "(1) *Where national law allows credit institutions, or groups of shareholders, or other persons in the course of their professional activities, or a company itself to invite shareholders to appoint them as proxies, Article 27 and the following provisions shall apply:*
(a) the appointment shall relate only to one meeting; it shall, however, be valid for successive meetings having the same agenda;
(b) the appointment shall be irrevocable;
(c) the invitation shall be addressed either in writing or by publication in one or more nationally distributed newspapers to every shareholder whose name and permanent address is known;
(d) the invitation must include the following at least:
(aa) the agenda indicating the items to be discussed and the proposals for decisions;
(cc) a statement to the effect that the documents referred to in Article 30 are available to any shareholder who requests them;
(dd) a request for instructions concerning the exercise of the right to vote in respect of each item on the agenda;
(ee) a statement of the way in which the proxy will exercise the right to vote if the shareholder gives no instructions;
(e) the right to vote shall be exercised in accordance with the statement made to the shareholder. This shall not, however, affect national laws which allow the proxy to depart from the instructions received or the statements made. In the event of any such departure, the proxy shall inform the shareholder.
(3) A Member State may provide that, contrary subparagraph 1(a), the appointment shall not relate to one or more general meetings having the same agenda but to specified period of not more than 15 months. In that event, the particulars listed in subparagraph 1(d) must be communicated

principle, the appointment of the proxy shall relate only to one meeting and the shareholder may give instructions concerning the exercise of the vote. If no instructions are given, the proxy is in principle obliged to vote in a way previously stated and made known to the shareholder. However, these provisions are considerably diluted by exceptions allowing the member states to provide that the proxy may depart from the instructions, if such were given, or his statement to the shareholder.¹¹¹ Moreover, member states may also provide that the appointment of a proxy shall not relate to a single general meeting, but to a period of not more than 15 months,¹¹² which would in effect often lead to the proxy having full discretionary power. It is therefore rather doubtful whether Article 28 would have a significant effect in terms of removing the barrier considered here. In fact, Article 28 is in essence very similar to the law as it stands at present in Germany.¹¹³

5.3. Concluding Remarks

Contemplating the European developments in terms of takeovers it appears that the emphasis has since the mid 1980s been clearly placed on the creation of a Takeover Directive regulating the takeover procedure and ensuring the equal treatment of shareholders rather than the removal of existing barriers. Whether the EC-Commission has in that respect got its priorities right seems questionable. As long as in some member states, like in Germany, structural barriers exist which most effectively prevent takeover bids, there seems - at least in respect of these countries - no point in having a takeover law regulating procedural aspects. British

to every shareholder referred to in subparagraph 1(c) before each general meeting."

111 Article 28(1)(e).

112 Article 28(3).

113 Sec. 135 AktG.

acquisitions in Germany would not substantially be facilitated simply by having a Takeover Directive. This is particularly true under the terms of the 1996 proposal the harmonizing effect of which would be minimal.

What is needed at the present stage are reinforced efforts to remove the existing barriers. When this is achieved, the need for a Takeover Directive will then arise automatically. Although the proposed 5th Directive takes some quite useful steps to tackle some of the most eminent barriers, especially since the second amendment of the 1988 version in 1991, the chance that this Directive will be adopted in the foreseeable future is more than dim. The reason being not so much the provisions concerning the takeover barriers, but the most controversial question of employee participation. Hence, a logical way forward would be to separate these different issues, i.e. to strike off the provisions regarding employee participation from the proposed 5th Directive and to return to them later in a different Directive.¹¹⁴ This approach, however, appears to have been rejected by the Commission, the result of which is that the prospects for the creation a "level playing field" in Europe remain bleak at present.

114 See also *Andenas*, The future of EC company law harmonisation, [1994] *Company Lawyer*, Vol. 15, No. 4, p. 121, 122; *Dine*, EC Company Law, para 8.1; *Palmer's Company Law*, para 16.403.

PART THREE

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Chapter 6

MERGER CONTROL IN BRITAIN

6.1. Introduction

Part Three of this work undertakes to explore the way in which takeovers and mergers are policed by the relevant public authorities in Britain, Germany and under the European jurisdiction. The relevant field of law, called merger control in Britain, concentration control in Brussels, and “Fusionskontrolle”, “Zusammenschlußkontrolle”, or “Kartellrecht” in Germany, is in all three jurisdictions regarded as part of the wider field of competition law. This classification gives by itself some information about the concern which lies at the heart of merger control law: competition. In a way, however, this categorisation is somewhat misleading as it is - at least in Britain - not only competition that matters.¹

Basically merger control is a form of governmental intervention in an otherwise lawful commercial transaction with the purpose of protecting the wider public.² Whereas the company law aspects of regulatory control over takeovers considered in Part Two of this work deal, broadly speaking, with the technicalities of making a bid and, in terms of substantive law, with the equal treatment of shareholders during the bidding process, thus the protection of private interests, merger control in Britain pursues a much wider and in a sense much

1 See Chapter 6.4.2. at pp. 254.

2 For a discussion on a fundamental level see *Kenneth George, Do we Need a Merger Policy?*, p. 281-300.

more difficult task. It undertakes - at least in principle - to evaluate the merits of a takeover or merger in order to establish, or rather prognosticate, whether a particular transaction "*operates, or may be expected to operate, against the public interest.*"³

The principal aim of Part Three of this work - beginning with Chapter 6 on merger control in Britain - is to analyse and compare the respective merger control procedures and to review and appraise the substantive public interest criteria applied by the relevant national and European authorities. It is proposed to highlight the main discrepancies between the respective regulatory systems along with the frictions arising from this, particularly in the case of international mergers. Where appropriate, suggestions will be made as to possible scope for reform.⁴

6.1.1. Historical Development

Unlike the self-regulatory system established under the City Code governing the acquisition of shares through takeover bids, public merger control in Britain is - and has always been - based entirely upon statutes.

Merger control in Britain formally begins with the enactment of the Monopolies and Mergers Act 1965. Although no power to control mergers existed prior to the 1965 Act, to fully understand the present system it is imperative to go back in time some further 17 years to the 1948 Monopolies and Restrictive Practices (Inquiry and Control) Act, with which modern competition law in the United Kingdom began.⁵ The 1948 Act set up the independent Monopolies and

3 Sec. 84 (1) FTA 1973.

4 See *Sir Bryan Carsberg*, Director General of the Office of Fair Trading, in *Times*, February 23, 1995.

5 For a thorough analysis of U.K. merger policy see *Fairburn*, *The Evolution of Merger Policy in Britain*, p. 193-230.

Restrictive Practices Commission,⁶ the early forerunner of today's Monopolies and Mergers Commission (MMC), consisting of businessmen, economists, trade unionists and lawyers. On referral by the Board of Trade, the Commission examined restrictive trade practices⁷ and manufacturing monopolies against a somewhat vague public interest criterion including inter alia business efficiency and competition.⁸

As the takeover activity increased sharply in the late 50s and early 60s - a development which also led to the Notes on Amalgamations of British Business (1959) and finally to the City Code on Takeovers and Mergers (1968)⁹ - the case for governmental control over mergers became widely accepted.¹⁰ The proposals made by the Conservative government in its 1964 White Paper¹¹ were largely adopted by the Labour government, which came into power in October 1964, and included in the Monopolies and Merger Act 1965. The 1965 Act itself was very much based on the 1948 Act, which by and large meant that the regulatory structure which had previously applied to monopolies was simply extended to mergers from that time on.¹² Henceforth, certain mergers¹³ could be referred by the Board of Trade to the Monopolies and Mergers Commission which then investigated whether the merger operated against the public interest.¹⁴ Contrary to the 1948 Act, however, the term "public interest" was not defined in the 1965 Act. Following an adverse finding by the Commission the Board of Trade was entitled

6 Sec. 4 (1) FTA 1973 still refers to the original 1948 Commission.

7 The investigation of restrictive practices was hived off from the Commission in 1956 by the Restrictive Trade Practices Act 1956.

8 Sec. 14 Monopolies and Restrictive Practices Act 1948.

9 See Chapter 3.1.1. at pp. 29 with further references.

10 *Fairburn*, The Evolution of Merger Policy in Britain, p. 194. Also *Whish/Sufrin*, Competition Law, p. 61.

11 Conservative White Paper: Monopolies, Mergers, Restrictive Practices, London 1964, Cmnd 2299.

12 Sec. 6-8 MMA 1965.

13 Qualifying for investigation were mergers leading to a market share of at least 1/3 or involving assets taken over worth more than £5 million over: sec. 6 (1)(b) MMA 1965.

14 Sec. 6 (2) MMA 1965.

to prohibit the merger or take other appropriate action.¹⁵

The basic regulatory framework established by the 1948 and the 1965 Acts has largely been confirmed by the Fair Trading Act 1973 (FTA 1973), which replaced the 1965 Act in toto and is the relevant piece of legislation today. Part V of the FTA 1973 distinguishes between “*newspaper merger references*”¹⁶ and “*other merger references*”.¹⁷ The provisions on “*other merger references*” apply in principle to all forms of merger and to any sector of industry. Apart from newspaper mergers, a number of specific provisions supplementing the Fair Trading Act are in force with regard to mergers involving water companies,¹⁸ building societies,¹⁹ banks,²⁰ and broadcasters.²¹ Concerning those special sectors a stricter merger control regime applies, which will not be discussed in detail in this chapter.²²

A number of minor amendments to the FTA 1973 were introduced by the Companies Act 1989 and the Deregulation and Contracting Out Act 1994. However, the basic structure and principles are still very much the same.

To sum up, the development of merger control in the United

15 Sec. 3 MMA 1965.

16 Sec. 57-62 FTA 1973. The reason for the specific provisions on newspaper mergers is the political sensitivity of the issues involved, namely the freedom of expression of opinion and the unbiased presentation of news.

17 Sec. 63-75 FTA 1973.

18 See sec. 32-34 of the Water Industry Act 1991. The MMC must have regard to the principle that the number of water enterprises under independent control should not be reduced so as to prejudice the ability of the Director General of Water Services to make comparisons between water companies. As to MMC reports so far see General Utilities plc/Colne Valley Water Company/Rickmansworth Water Company, Cm 1929 (1990); General Utilities plc/Mid Kent Water Company, Cm 1125 (1990); Southern Water plc/Mid Sussex Water Company, Cm 1126 (1990); Lyonnaise des Eaux SA/Northumbrian Water Group plc, Cm 2936 (1995).

19 Sec. 93-95 Building Societies Act 1986.

20 Sec. 21 Banking Act 1987.

21 Sec. 2 Broadcasting Act 1990.

22 In principle newspaper and water industry mergers are automatically referred to the MMC contrary to the ordinary procedure where the Secretary of State enjoys a very wide discretion whether to refer or not.

Kingdom has shown a remarkable continuity as far as the legislative framework is concerned. In the following chapter it is proposed to analyse the current regime in some depth. Particular emphasis will be given to the question whether calls for reform are justified or not.²³

6.1.2. Overview over the Merger Control Process

The complexity of the British merger control process makes it necessary to provide a brief overview over the regulatory framework before embarking on a more detailed analysis of particular aspects of the decision-making process. The merger control process involves in principle three different institutions, each of which plays an entirely different role:

- (1) The Director General of the Office of Fair Trading (DGFT)
- (2) The Monopolies and Mergers Commission (MMC)
- (3) The Secretary of State for Trade and Industry

In a nutshell, the Director General of the Office of Fair Trading (DGFT) has the duty to monitor the takeover and merger activity across the country and advise the Secretary of State on whether a

23 See quite spectacular and fundamental criticism by *Sir Bryan Carsberg*, Director General of the Office of Fair Trading, in his evidence to the *Trade and Industry Committee*, see *Times*, February 23, 1995 and the *Trade and Industry Committee*, Fifth Report: U.K. Policy on Monopolies, 1995, Evidence February 22, 1995, p. 30; also *Hutchings*, The Need for Reform of U.K. Competition Policy, [1995] 4 ECLR 211; *Pratt*, Changes in U.K. Competition Law: A wasted Opportunity? [1994] 2 ECLR 89, 94. Also *Trade and Industry Committee*, First Report, Takeovers and Mergers, 1991, paras 284 et seq; with muted criticism *Finbow/Parr*, U.K. Merger Control, p. 323-336.

merger meets the qualifying criteria set out in the FTA 1973²⁴ and should be referred to the MMC.²⁵ As a more flexible alternative to suggesting reference or clearance the DGFT may also propose to the Secretary of State to seek an undertaking with the merging parties remedying the identified adverse effects of the merger in lieu of a reference.²⁶

The Secretary of State, who is not bound by the advice given to him by the DGFT, decides on a discretionary basis whether to refer or clear the merger, or accept undertakings in lieu of reference.

Merger references can be made both before²⁷ and after²⁸ a merger has taken place. If a reference is made, the MMC investigates the transaction in depth in order to establish whether the merger qualifies for investigation,²⁹ and if so, whether it operates, or may be expected to operate, against the public interest.³⁰ Its findings are published in most informative reports.³¹ In its reports the MMC specifically recommends what further course the Secretary of State should take.

If the merger does not qualify for investigation or if no adverse effects on the public interest are to be expected, the merger is automatically cleared, and the Secretary of State has no further role to play. In the event of an adverse MMC report, however, the Secretary of State may clear the merger or interfere with it in such a way as he considers requisite for the purpose of remedying or preventing the adverse effects specified in the MMC report.³² He

24 See Chapter 6.2. at pp. 214.

25 Sec. 76 FTA 1973.

26 Sec. 75G-75K FTA 1973.

27 Sec. 75 FTA 1973.

28 Sec. 64 FTA 1973.

29 As to the relevant criteria see Chapter 6.2. at pp. 214.

30 Sec. 69, 84 FTA 1973. See Chapter 6.4. at pp. 245.

31 An up-to-date list of all reports may be obtained from the MMC, New Court, 48 Carey Street, London WC2A 2JT. Reports are available from HMSO Publications Centre, PO Box 276, London SW8 5DT.

32 Sec. 73 (2) and Schedule 8 of the FTA 1973. *R v. Secretary of State, ex parte Anderson Strathclyde plc* [1983] 2 All ER 233, 242.

may, for example, forbid a proposed or dismantle an implemented merger. If the Secretary of State decides to forbid a proposed merger, each House of Parliament has the opportunity to veto his decision; if he orders the dismantling of a completed merger, each House of Parliament must approve of this decision by majority vote.³³ Alternatively, the Secretary of State may ask the DGFT to seek undertakings in lieu of such orders from the merging parties with a view to remedying the adverse effects of the merger by this means.³⁴

Reflecting upon the British merger control system as outlined above two features in particular seem worthy of note and further examination:

(1) First, the tripartite institutional structure - OFT, MMC and Secretary of State - of the British merger control process. In the evidence recently given before the Trade and Industry Committee the MMC admitted that it is "*not aware of any state which has a tripartite structure like ours.*"³⁵ The U.K. system certainly contrasts sharply with the German³⁶ and European³⁷ regulatory frameworks, both of which favour a unitary system where - in principle - a single body is in charge from A to Z. The question arises whether the inherited British merger control structure, which has been in place for quite some time now, is still able to meet the demands of an effective and efficient merger control process in a modern capitalistic economy. On the face of it, at least, a unitary system where only one authority is involved in the decision-making process from the beginning on appears to be simpler. Before coming to any conclusions on these questions the pro's and con's of the respective systems will be carefully considered in the following chapters.

33 Sec. 91, 134 FTA 1973.

34 Sec. 88 FTA 1973.

35 *Trade and Industry Committee*, Fifth Report, 1995, para 127; evidence p. 22.

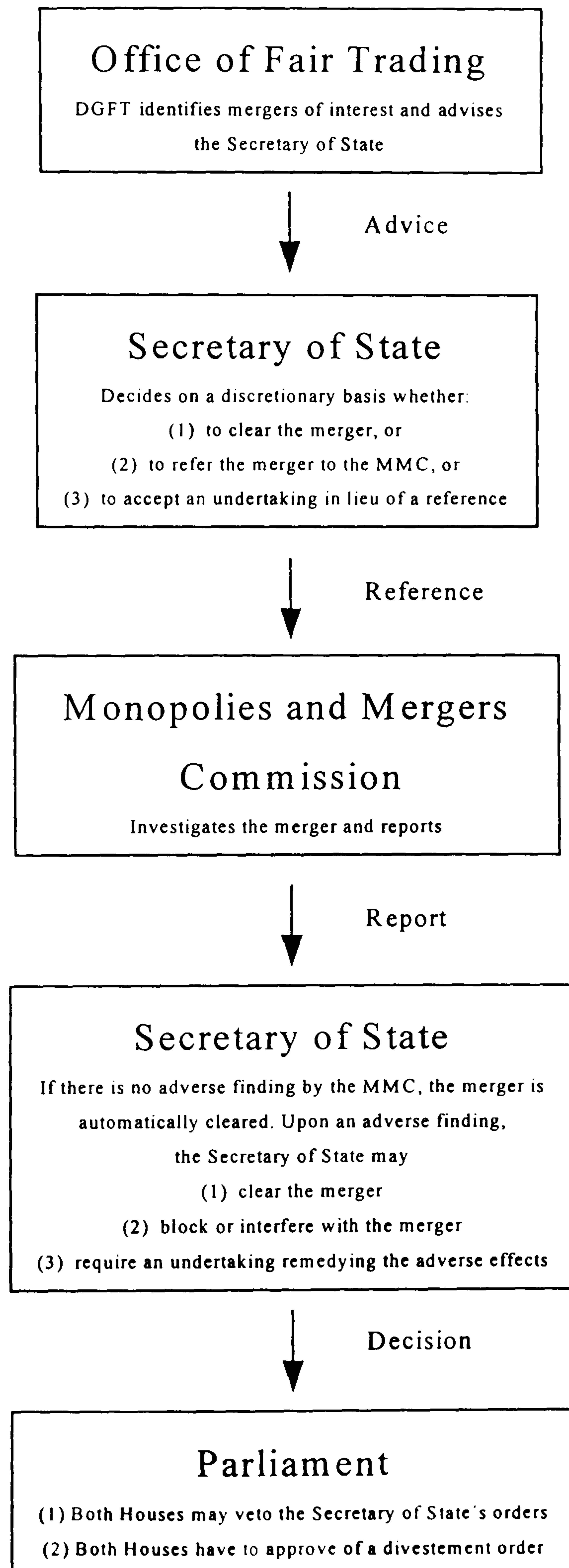
36 See Chapter 7 at pp. 265.

37 See Chapter 8 at pp. 335.

(2) The second point of particular interest from a comparative point of view is the key-role played by the Secretary of State within the merger control process. It is the Secretary of State who decides in a "*filtering function*"³⁸ on a discretionary basis whether a merger is to be referred to the MMC in the first place. Mergers he does not want to be scrutinized are not referred and go through. If a reference has been made by him and the MMC reports adversely, it is again the Secretary of State who then takes the final decision. The institutional and policy question arising is whether it is appropriate that the decision making power lies almost exclusively with a government minister rather than a politically independent body or person. In terms of substantive merger policy, it will be interesting to examine if, and to what degree, merger decisions are because of this institutional structure motivated by political considerations.

In order to come to any substantiated conclusions on the points raised, it is necessary to examine the crucial stages and the underlying philosophy of the decision-making process in Britain more closely.

38 Goyder, *Public Interest Criteria*, Fordham 1994, p. 125, 129.



6.2. Mergers Qualifying for Investigation

In order to qualify for investigation a business transaction has to meet certain qualitative and quantitative criteria provided for in the Fair Trading Act:

- (1) The transaction must constitute a merger as defined by the Act (6.2.1.).
- (2) In terms of quantity, the merger must either satisfy a market share or assets test (6.2.2.).
- (3) The merger must have taken place not more than six months before the reference is made (6.2.3.).
- (4) There must be a territorial link to the U.K. (6.2.4.)

6.2.1. Definition of a Merger

In the commercial reality the term merger is used for a wide range of transactions, encompassing, for example, public takeover bids, the purchase of shares on the Stock Exchange, the acquisition of assets, joint ventures, management buy-outs, reconstructions and amalgamations. The Fair Trading Act, flexibly taking account of the commercial diversity of transactions,³⁹ defines mergers in broad terms leaving wide discretion to the relevant authorities.⁴⁰ Under section 64 (1) of the Act a merger is deemed to exist where “*two or more enterprises have ceased to be distinct enterprises.*”

39 Stagecoach Holdings Plc/Lancaster City Transport Ltd, Cm 2423, 1993, para 6.21.

40 See *OFT, Mergers. A guide to the procedures under the FTA 1973*, p. 3.

The term “enterprise” is defined as *“the activities, or part of the activities, of a business”*⁴¹ comprising any form of identifiable business regardless of the legal status of the acquired business.⁴² The purchase of a factory including equipment, employees, customers, suppliers and goodwill would undeniably amount to the acquisition of an enterprise.

Broadly speaking, enterprises *“have ceased to be distinct enterprises”* where control of one has passed to the controller of the other.⁴³ Of central importance is, hence, the notion of “control”. Section 65 (3) stipulates that *“a person or group of persons able, directly or indirectly, to control or materially to influence the policy of a body corporate, or the policy of any person in carrying on an enterprise, but without having a controlling interest in that body corporate or in that enterprise, may be treated as having control of it.”* Three categories of control can be derived from the wording of this section:

- (1) A controlling interest
- (2) Ability to control policy
- (3) Ability materially to influence policy

The term “controlling interest” is well-defined in company law terms, meaning a shareholding carrying more than 50 cent of the voting rights.⁴⁴ What is meant by the ability *“to control or materially to influence the policy”* of another enterprise is far more difficult to establish both in theory and practice. These terms are not defined by the Act and have no direct equivalent in company law. The OFT

41 Sec. 63 (2) and 137 (2) FTA 1973.

42 *Butterworth's Competition Law*, Div. VII, para 62. Also AAH Holdings/Medicopharma NV, Cm 1950, 1992, para 6.69; Stagecoach Holdings Plc/Lancaster City Transport Ltd, Cm 2423, 1993, para 6.21.

43 *Butterworth's Competition Law*, Div. VII, para 66; *Finbow/Parr*, U.K. Merger Control, para 2.007.

44 OFT, Mergers. A guide to the procedures under the FTA 1973, p. 5.

declared that a view “*has to be taken case by case in the light of the particular circumstances.*”⁴⁵ Of course - but what does that mean? Much depends upon how widely the shares are dispersed⁴⁶ and on the de facto balance of power between the merging enterprises.⁴⁷ In the merger between *P & O* and *European Ferries*, the ‘leading case’ for this matter,⁴⁸ the stake acquired by *P & O* in *European Ferries* effectively amounted to only 16.1 per cent of the voting stock, but the MMC pointed out that no other shareholder controlled more than 5 per cent and that *P & O* had good connections with most institutional shareholders, which probably enabled it to block any resolution of which it disapproved.⁴⁹ It has been indicated by the OFT that a shareholding in excess of 15 per cent is liable to be examined to see whether the holder is able materially to influence policy. A stake of 25 per cent or more, which confers on the holder the power to block special resolutions, is almost certain to be seen as conferring power materially to influence policy. Above that stage a shareholder may already have the ability to control policy, i.e. de facto control. If a person moves from one category of control to another, for example from the ability materially to influence policy to the ability to control policy, this step qualifies again for

45 OFT, Mergers. A guide to the procedures under the FTA 1973, p. 5.

46 The Peninsular and Oriental Steam Navigation Company/European Ferries Group plc, Cm 31, 1986, para 8.6.; Government of Kuwait/BP, Cm 477, 1988, para 8.16.

47 Stagecoach Holdings plc/S.B. Holdings Ltd, Cm 2845, 1995, para 2.38: “Stagecoach is the biggest operator of bus services in the U.K., with ver broad experience in the industry and an impressive record of growth, efficiency and profitability. SBH, although a substantial operator, is much smaller and weaker than Stagecoach and will be willing to be advised by Stagecoach on how to improve its performance.”

48 Comparable cases, albeit involving a higher stakes, are Eurocanadian Shipholdings/Furness Withy/Manchester Liners, HC 639, 1976 (28.8 %); GUS/Empire Stores, Cmnd 8777, 1983 (29.99 %); Pleasurama/Trident/Grand Metropolitan, Cmnd 9108, 1983 (20.02 %); Lonrho/House of Fraser, Cmnd 9458, 1985 (29.9 %); Government of Kuwait/BP, Cm 477, 1988, (21.6 %); recently: Stagecoach Holdings plc/S.B. Holdings Ltd, Cm 2845, 1995(20 %).

49 The Peninsular and Oriental Steam Navigation Company/European Ferries Group plc, Cm 31, 1986, para 8.6.

investigation.⁵⁰ Thus a particular transaction may qualify up to three times if the acquisition is made by stages.

6.2.2. Quantitative Criteria

In terms of size the Fair Trading Act demands either an “asset test” or a “market share test” to be met.

The assets test is satisfied where the gross value of the world-wide assets taken over exceeds £70 million.⁵¹ Most merger references are made on the basis of the assets test since it is much easier for the authorities to ascertain whether this test is satisfied.⁵²

The market share test is satisfied if the merger results in a market share of at least 25 per cent of goods or services of any description in the United Kingdom or in a substantial part⁵³ of it for the merging enterprises.⁵⁴ To identify the relevant market and determine the size of a market share is inherently difficult and requires not only precise data, but depends also very much on how the market is defined in terms of the relevant product (substitutability analysis) and geographic market.⁵⁵ To facilitate this task for the competition authorities at the qualifying stage, the Fair Trading Act allows for wide discretion:⁵⁶

50 *Butterworth's Competition Law*, Div. VII, para 66.

51 Sec. 64 (1)(b) FTA 1973. See Increase in Value of Assets Order 1994, SI 1994/72).

52 *Whish/Sufrin*, Competition Law, p. 682.

53 What is meant by substantial part of the U.K. has been the subject of a House of Lords decision: *R. v. MMC*, ex parte South Yorkshire Transport Limited [1993] 1 All ER 289, 297: “the part must be of such size, character and importance as to make it worth consideration for the purposes of the Act.”

54 Sec. 64 (1)(b) and (2),(3) FTA 1973.

55 *Finbow/Parr*, U.K. Merger Control, para 2.014.

56 See *OFT*, Mergers: A guide to the procedures under the Fair Trading Act 1973, para 13. Also *Raybould/Firth*, Comparative Law of Monopolies, Pt. II 4.4.2. p. 454.

*“.... the Secretary of State or the Commission, as the case may be, shall apply such criterion (whether it be value or cost or price or quantity or capacity or number of workers employed or some other criterion, of whatever nature) or such combination of criteria as may appear to the Secretary of State or the Commission to be most suitable in all the circumstances.”*⁵⁷

The assets/market share approach employed in Britain differs from the qualifying criteria applied under German⁵⁸ and European⁵⁹ merger control law. There, the quantitative qualification is based on the turnover of the parties involved. While the British approach is probably more to the point as the asset and market share test relate directly to the merger itself, the turnover based calculation in Europe and Germany may be easier to handle in practice as the turnover figures are set out in the balance sheets of the enterprises involved.

6.2.3. Time Limit

A merger reference, if it is made after the merger has taken place, can only be made within a six months period after the date the enterprises have ceased to be distinct.⁶⁰ However, the six months period will not begin to run unless the merger has been “*made public*”.⁶¹ The term “*made public*” is defined as being so publicized (in the financial press) as to be generally known or readily ascertainable.⁶²

57 Sec. 68 (3) FTA 1973.

58 See Chapter 7.3.2. at pp. 293.

59 See Chapter 8.3.2. at pp. 362.

60 For more details see *Finbow/Parr*, U.K. Merger Control, para 2.018.

61 Sec. 64 (4) FTA 1973.

62 Sec. 64 (9) FTA 1973.

6.2.4. Territorial Link

As a matter of course, a merger may only be investigated by the U.K. authorities if there is some U.K. link.⁶³ The Fair Trading Act requires that of the merging enterprises “*one at least was carried on in the United Kingdom or by or under the control of a body corporate incorporated in the United Kingdom.*”⁶⁴ Hence, a merger between two foreign companies may be investigated if one of the enterprises has a U.K. subsidiary, branch or a representative office.⁶⁵ An example of this constellation is the merger between *MiTeK Industries Inc* and *Gang-Nail Systems Inc*, both of which were incorporated in the U.S.⁶⁶ However, each of the corporations had a subsidiary operating in the U.K., namely *Hydro-Air Ltd* and *Gang-Nail Systems Ltd*. The U.S. merger between the parents would have resulted in the subsidiaries together having a market share of 76 per cent in the U.K., which prompted the MMC to recommend that MiTeK should divest itself of *Gang-Nail Systems Ltd*. A number of the MMC’s reports have dealt with mergers involving foreign companies,⁶⁷ but the jurisdictional question as such appears, contrary to experiences in Germany,⁶⁸ never to have caused a problem in practice.⁶⁹ The definition, in particular the phrase enterprise “*carried on in the*

63 For a more general analysis of the issue see: Lowe, Extraterritorial Jurisdiction. The British Practice, *RabelsZ* 1988, 157 et seq.

64 Sec. 64 (1) FTA 1973. In its publication, *Mergers: A guide to the procedures under the FTA 1973*, the OFT states on p. 3: “*at least one of the enterprises must be carried on in the United Kingdom or by or under the control of a body corporate incorporated in the United Kingdom. This means that a merger between two foreign companies may still qualify for investigation where either company controls any enterprise which is carried on or incorporated in the United Kingdom.*”

65 *Butterworth’s Competition Law*, Div. VII, para 63.

66 *MiTeK Industries Inc and Gang-Nail Systems Inc*, Cm 429, 1988.

67 For an appraisal of the substantive issues involved in the context of foreign companies see Chapter 6.4.2.(2) at pp. 258.

68 See Chapter 7.3.3. at pp. 295.

69 *Butterworth’s Competition Law*, Div. VII, para 64.

U.K.”,⁷⁰ seems wide enough to catch any transaction in which the U.K. could possibly have an interest.⁷¹

It should be noted, however, that the Secretary of State's power⁷² to make orders against foreign firms is strictly limited by section 90(3) of the FTA 1973 which stipulates that he may not take any formal extraterritorial action against foreign enterprises.

6.3. Procedural Aspects

The following paras intend to examine those procedural features which are determinative to the British merger control process. As it is not possible within the scope of this work to provide an exhaustive description of every procedural detail of the quite sophisticated merger control process in Britain,⁷³ the following representation will concentrate on certain aspects which appear of particular interest both from a comparative point of view and in respect of the ongoing debate in Britain.⁷⁴

70 It is not entirely clear what is meant by this expression, in particular whether the mere sale of products by an overseas enterprise which has no permanent place of business in the U.K. would satisfy the territorial link requirement. See *Finbow/Parr*, U.K. Merger Control, para 2.012; *Butterworth's Competition Law*, Div. VII, para 63.

71 As to the territorial aspects under European law see Chapter 8.3.2.(2) at pp. 365.

72 As to the powers of the Secretary of State see section 73 and Schedule 8 of the FTA 1973.

73 For a precise and up-to-date description of the merger control procedure refer to *Finbow/Parr*, U.K. Merger Control, 1995; also *Freemann/Whish*, *Butterworth's Competition Law*, Division VII, 1994.

74 See in particular the Reports of the *Trade and Industry Committee*, First Report, Takeovers and Mergers, 1991; Fifth Report: U.K. Policy on Monopolies, 1995. Also the Annual Report of the DGFT 1994. *Hutchings*, The Need for Reform of U.K. Competition Policy, [1995] 4 ECLR 211; *Pratt*, Changes in U.K. Competition Law: A wasted Opportunity? [1994] 2 ECLR 89, 94.

6.3.1. The OFT Procedure

The Director General of the Office of Fair Trading (DGFT) heads the Office of Fair Trading, which is a non-ministerial government department established by the FTA 1973.⁷⁵

(1) Function of the OFT

As has been pointed out earlier, the basic statutory function of the DGFT in relation to merger control is to keep himself informed of actual and anticipated merger activity⁷⁶ and advise the Secretary of State as to possible references. The need for such a "watchdog" is at least partly due to the fact that, unlike Germany⁷⁷ and the EC,⁷⁸ Britain has no legal requirement that the parties to a merger should notify the merger control authorities or seek clearance before implementing the merger.⁷⁹ Hence, the merger control authorities do not automatically know about ongoing mergers. This illustrates the liberal attitude taken by the Fair Trading Act towards controlling mergers. To compensate for this "procedural disadvantage" of the OFT, the Secretary of State has power to refer a completed merger, if he believes it qualifies, within six months of its having taken place and being made public to the MMC.⁸⁰ The OFT may learn of a merger from the financial press, other government departments, or voluntarily from the merging parties themselves, or third parties with

75 Address: Field House, 15-25 Bream's Buildings London EC4A 1PR. For a description of the OFT's work by the director of the Competition Policy Division of the OFT see: *Martin Howe*, U.K. Merger Control: How does the System Reach Decisions? A Note on the Role of the Office of Fair Trading, [1990] 1 ECLR 3-10.

76 Sec. 76 (1)(a) FTA 1973.

77 Sec. 24a (1) GWB.

78 Art. 4 of the Regulation 4064/89.

79 As to the pro's and con's of pre-notification see *DTI*, Blue Paper on Mergers Policy, para 3.1-3.17.

80 Sec. 64 (4) FTA 1973. See 7.2.3.

an interest, for example competitors or consumer protection groups. The absence of a mandatory pre-notification requirement has been criticized by the Trade and Industry Committee for being too "*informal and uncertain*".⁸¹ They recommended that pre-notification should be made mandatory where assets of more than £30 million are involved.⁸² Although *Sir Gordon Borrie*, the DGFT at that time, is probably right in saying in his evidence to the Trade and Industry Committee that it is rather unlikely that any merger which would result in serious detriments to the public interest would escape the notice of the OFT,⁸³ a pre-notification requirement would facilitate the policing of mergers and the additional "administrative burden" on companies does not seem unreasonable provided that the notification threshold is high enough to catch only large deals. The £30 million threshold proposed by the Trade and Industry Committee appears to make sense.

A *voluntary* pre-notification system has been introduced in Britain by the Companies Act 1989⁸⁴ which amended section 75 of the FTA 1973. This new procedure has so far received a reserved reception, with numbers declining (1990: 51 pre-notification cases; 1995: only 11).⁸⁵

As far as OFT proceedings are concerned a number of options are available to the merging parties:

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- 81 *Trade and Industry Committee*, First Report on Takeovers and Mergers, 1991, para 79, 80.
 - 82 The pre-notification requirement in Germany and the EU is primarily based on the turnover of the merging parties, not on the assets taken over.
 - 83 See the evidence given by *Sir Gordon Borrie*, DGFT of the day, to the *Trade and Industry Committee*, First Report, para 78, Question 823.
 - 84 Section 146 of the CA 1989. For more details see *The Merger (Pre-Notification) Regulations 1990* (S.I. 1990 No. 501). A special form called "*Office of Fair Trading Merger Notice*" for notifying the DGFT has been issued by the OFT.
 - 85 See Table 10 at p. 224, column 4.

- (a) Not to seek clearance at all, i.e. to risk intervention
- (b) Confidential guidance prior to a merger
- (c) Voluntary pre-notification
- (d) Traditional written submission
- (e) Undertaking in lieu of reference (where adequate)

Each of these procedures has its strengths and weaknesses which cannot be discussed here.⁸⁶ Suffice it to say that the right choice of procedure very much depends on the concrete situation and often involves an element of tactic.⁸⁷ Table 10 at page 224 provides some information as to the workload of the OFT and the choice of procedure in practice. Quite remarkable is the gap between the high number of cases first examined and the very small number of cases in respect of which a reference to the MMC is finally recommended. These figures indicate that merger control in Britain is exercised in a rather liberal way.

86 Useful information is provided by the OFT's publication *Mergers: the Content of Submission*. A note by the Office of Fair Trading, March 1994.

87 For an excellent analysis of the considerations to which the parties should have regard to in making this choice see *Finbow/Parr*, U.K. Merger Control, Chapter 3.

Table 10: OFT Workload

Year	Cases examined	Qualifying cases	Pre-merger notification	Confidential guidance	Reference recommended
1986	524	313	--	55	15
1987	478	321	--	40	6
1988	456	306	--	45	11
1989	427	281	--	32	14
1990	369	261	51	22	21
1991	285	183	38	15	8
1992	200	125	9	21	10
1993	309	197	13	46	5
1994	381	231	7	76	8
1995	473	275	12	107	11

Source: Annual Reports of the DGFT

(2) Personnel and Resources

Among the various functions of the OFT merger control accounts for only a relatively small part of its work. According to the Annual Report 1994 the OFT spent in 1994 only 4 per cent of its £19.6 million budget directly on merger control.⁸⁸ The Mergers Secretariat, the subdivision of the OFT charged with the administration of mergers, is relatively small comprising in 1993 the

88 Allocation of OFT resources: Regulatory: 26%; Information: 16%; Restrictive trade practices: 13%; Consumer policy: 12%; Monopolies and anti-competitive practices: 11%; Economics: 8%; Legal: 7%; Mergers 4%; International: 3%.

head of the Secretariat, two principal case officers and four other case officers, four economists, a lawyer, and six support staff.⁸⁹

Given these limited resources both financially and personnel-wise, it is obvious that the merger investigations undertaken by the Mergers Secretariat of the OFT can only be of a rather superficial and cursory nature.⁹⁰ This is admitted by the DGFT in his 1994 Annual Report himself:

*"My information-gathering powers give me limited ability to make a fully rounded judgement of whether or not anti-competitive behaviour is working significantly against the public interest. When I propose making a reference, the company or companies concerned may tell me that they would prefer to change their behaviour rather than bear the costs and other detrimental consequences of a reference. But this is difficult for me because, without undertaking a more detailed investigation than is possible for me, I lack confidence in judging what changes are needed to deal with the situation."*⁹¹

Under the present institutional structure it is, of course, the MMC's function to carry out the in-depth investigation. The question is, however, whether it makes sense to split the investigation process in this way. While it is comprehensible that the procedure is as such split in a preliminary and an in-depth examination, it is more difficult to understand why these stages should be performed by different institutions and different people. If one authority only were charged with investigating mergers, as it is the case in Germany, the EC, and many other countries, the same people would deal with the merger from the very beginning on and knowledge about the merger could

89 *Finbow/Parr*, U.K. Merger Control, paras 1.003 and 3.028 et seq. As to critical remarks on the calibre of the OFT staff in general see *Trade and Industry Committee*, First Report, para 104 et seq. A problem appears to be that Civil Service salary constraints make it difficult for the OFT (and the MMC) to attract high-quality staff from outside the public sector.

90 See also *Trade and Industry Committee*, First Report, para 287 et seq.

91 *Sir Bryan Carsberg*, Annual Report 1994, p. 15.

build up from the very first day. Under the present system, however, the investigative process is interrupted when a reference to the MMC is made. To some degree the work done by the OFT is duplicated by the MMC. From the companies' point of view dealing with only one authority throughout the procedure is preferable to the present situation. Given the DGFT's own admission that he is not able to "*make a fully rounded judgement*" and given the fact that the MMC procedure is very expensive and time consuming for the companies involved, it is questionable whether a decision as important as a reference decision by the Secretary of State, should be based on such inherently limited advice.

(3) Policy of the DGFT

Surprisingly, there is no provision contained in the FTA 1973 stipulating the matters the DGFT has to take into account when making his recommendation.⁹² Section 84 of the FTA 1973, which refers to the public interest, is directly addressed to the MMC only.⁹³ It is, however, tacitly accepted by everybody involved that the criteria applicable by the MMC must be equally relevant to the DGFT.⁹⁴

An analysis of the recommendation policy of the DGFT is impeded by the fact that the reasons for a recommendation are not publicized.⁹⁵ The DGFT submits a summary of the main features of the merger and those issues of particular concern to the Secretary of State. The DGFT has in the past declared that in making his recommendation he would have regard to the current publicly-stated

92 *Raybould/Firth*, Comparative Law of Monopolies, Pt. II 4.4.1. p. 449.

93 See Chapter 6.3.3.(3) at pp. 239.

94 *Sir Gordon Borrie* in his evidence given to the *Trade and Industry Committee*, First Report, para 254 and Q 796.

95 *Goyder*, Public Interest Criteria, Fordham 1994, p. 125, 129.

government policy. This dependence on government policy has led to harsh criticism by the Trade and Industry Committee:

*"...by accepting that he does choose to operate within stated government policy, Sir Gordon Borrie [the DGFT at that time] is, in our view, both limiting his independence and compromising the integrity of the advice he gives."*⁹⁶

On the other hand, the Secretary of State is not bound by the DGFT's advice anyway. Were the DGFT not to take account of the government policy of the day, the result would simply be a more frequent divergence between the Secretary of State's reference decision and the advice given to him by the DGFT.⁹⁷ The whole concept of the DGFT's independence is somewhat feeble as the DGFT is appointed by the Secretary of State.⁹⁸ Given the relative lack of transparency at this stage of the process,⁹⁹ the DGFT following the government's policy is at least conducive to certainty and predictability and, thus, in the interests of industry.

(4) Timing

The general position under the Fair Trading Act 1973 is that a completed merger cannot be referred to the MMC by the Secretary of State if it has taken place and made public at least six months previously.¹⁰⁰ This limits the period of uncertainty for those companies who decide to go ahead with a merger without seeking clearance.

⁹⁶ Trade and Industry Committee, First Report, para 254.

⁹⁷ Sir Gordon Borrie, Trade and Industry Committee, First Report, para 255 and Q 274.

⁹⁸ Sec. 1 (1) FTA 1973. He can, however, only be removed by the Secretary of State on the grounds of incapacity or misbehaviour.

⁹⁹ Goyder, Public Interest Criteria, Fordham 1994, p. 125, 129.

¹⁰⁰ Sec. 64 (4) FTA 1973.

Within this six-months-period the administrative timetables under which the DGFT has to operate differ according to the chosen procedure.

(a) *Confidential Guidance*. In the non-statutory confidential guidance cases, the DGFT aims to advise the Secretary of State within 19 working days, which should ensure that the Secretary of State's reference decision is reached within 25 working days overall.¹⁰¹

(b) *Pre-notification*. Under the statutory pre-notification procedure the Secretary of State must reach his decision within 20 working days with the possibility of a single extension of 15 working days.¹⁰² To allow the Secretary of State time to reach his decision, the DGFT has to submit his advice a few days earlier.

(c) *Traditional written submission*. In traditional non-pre-notification cases no particular statutory time limit is imposed on the DGFT apart from the six months period mentioned above. The DGFT has announced, however, that he aims to offer his advice within 39 working days which should enable the Secretary of State to come up with a decision within 45 working days.¹⁰³

Hence, whichever procedure is chosen a couple of weeks elapse until the DGFT is ready to submit his advice. It is submitted that some of this time could be saved if a single authority were to investigate mergers. It remains to be seen, however, whether the German unitary model works better in practice.¹⁰⁴

101 *OFT, Mergers: the Content of Submissions*, March 1994, p. 1.

102 Sec. 75B(2)(3) FTA 1973. *Merger Prenotifications Regulations* 1994, SI 1994/1934. See *Annual Report of the DGFT* 1994, p. 41.

103 *OFT, Mergers: the Content of Submissions*, March 1994, p. 1.

104 Chapter 7 at pp. 265.

6.3.2. The Secretary of State's Reference Decision

The Fair Trading Act 1973 is silent as to the grounds upon which the Secretary of State should base his reference decision. It is generally accepted, however, that the Secretary of State should be guided by the broad criteria set out in section 84 of the Fair Trading Act, which are directly addressed only to the MMC.¹⁰⁵ Given the absence of clear reference criteria in the Act and the fact that the Secretary of State is not legally bound by the advice given to him by the DGFT, it is clearly the policy of the Act to vest the widest possible discretion in the Secretary of State.¹⁰⁶ This was confirmed by the House of Lords in *Lonrho plc v. Secretary of State* in connection with the House of Fraser saga, where *Lonrho* unsuccessfully challenged the decision of the Secretary of State *not* to refer the successful bid by the *Al Fayed* brothers for *House of Fraser*, i.e. *Harrods*, to the MMC.¹⁰⁷

In practice, the Secretary of State relies heavily on the advice given to him by the DGFT and divergencies are rather scarce as Table 11 below indicates.

105 *Lonrho plc v. Secretary of State*, [1989] 2 All ER 609, 617. *OFT*, Mergers: A guide to the procedures under the Fair Trading Act 1973, p. 7.

106 *Finbow/Parr*, U.K. Merger Control, para 4.001: "As a matter of law, however, the Secretary of State has an almost unlimited discretion in deciding whether to refer a merger to the MMC." Also *Whish/Sufrin*, Competition Law, p. 686.

107 *Lonrho plc v. Secretary of State*, [1989] 2 All ER 609, 617.

Table 11: Recommendation and Reference¹⁰⁸

Year	Reference recommended by DGFT	Reference recommended but not made by S.o.S.	Reference made, but not recommended by S.o.S.	Total references made by the S.o.S.
1986	15	2	--	13
1987	6	--	--	6
1988	11	--	--	11
1989	14	--	--	14
1990	21	--	4	25
1991	8	1	--	7
1992	10	--	--	10
1993	5	2	--	3
1994	8	--	--	8
1995	11	2	--	9

Source: Annual Reports of the DGFT

In view of the wide discretion enjoyed by the Secretary of State there have been complaints about a lack of predictability regarding the reference policy.¹⁰⁹ This appears to be true as far as competing bids are concerned, as the recent battle for the submarine maker *VSEL* by *BAe* and *GEC* demonstrates. Whereas the City confidently expected the rivalling bids to be cleared,¹¹⁰ the Secretary referred both. This was understandable and in line with the DGFT's advice as far as *GEC's* bid was concerned since competition concerns

¹⁰⁸ These figures do not include newspaper references.

¹⁰⁹ *Whish/Sufrin*, Competition Law, p. 687; Also *John Swift*, Merger Policy: Certainty or Lottery?, p. 264, 279 et seq, who concludes that merger policy is more predictable than is generally acknowledged.

¹¹⁰ *Financial Times*, December 8, 1994.

arose.¹¹¹ BAe's bid, however, was referred on the ground of "*public interest involving national security*". The Financial Times suggested that "*this phrase may more accurately be read as 'political expediency'*".¹¹² Accordingly, the MMC did not identify any adverse competition or other public interest consequences in BAe's case.¹¹³ Clearly, competing bids put the Secretary of State in a difficult position. Contrary to the BAe/GEC/VSEL case it has so far been publicly stated government policy to consider each bid independently.¹¹⁴ However, if one bid is cleared and the other referred, this may easily lead to complaints about discrimination and a distortion of market forces. To either refer or clear both bids may appear to be the easy way out from the Secretary of State's point of view - a view which he apparently took in the BAe/GEC/VSEL case. However, to refer a company unjustifiedly in order to avoid reaching a politically difficult decision, seems too heavy a price to pay from that company's point of view.¹¹⁵

Apart from the difficult issue of competing bids and some uncertainty in connection with foreign state-controlled bidders,¹¹⁶ the successive Secretaries of State have at least since the so called Tebbit-Doctrine¹¹⁷ in 1984 by and large pursued a fairly consistent

111 See the adverse finding by the MMC in May 1995: The General Electricity Company plc and VSEL, Cm 2852.

112 *Financial Times*, December 8, 1994.

113 British Aerospace Public Limited Company and VSEL plc, May 1995, Cm 2851.

114 The DTI, Blue Paper on Mergers Policy deals specifically with that problem in para 2.28 and Annex F: "The blocking of rival bids, in an attempt to remove the unfairness and distortion created by the original reference decision, would create further distortion and unfairness, not least to the bidder who finds his bid blocked although it is in itself unobjectionable." Also *Finbow/Parr*, U.K. Merger Control, para 4.016.

115 DTI, Blue Paper on Mergers Policy deals specifically with that problem in para 2.28 and Annex F.

116 See Chapter 6.4.2(2) at pp. 258.

117 *Lord Tebbit* in reply to a Parliamentary Question on July, 5, 1984: "I regard mergers policy as an important part of the Governments's general policy of promoting competition within the economy in the interests of the customer and of efficiency and hence of growth and jobs. Accordingly, my policy has been and will continue to be to make references primarily on competition grounds..."

reference policy focusing mainly on competition aspects.¹¹⁸ The various issues taken into account over the years will be considered at a later stage.¹¹⁹

Given the concurrence between the Secretary of State's reference decisions with the advice he receives from the DGFT one could raise the question whether it is necessary and expedient for the Secretary of State to be involved at this stage of the procedure at all. Why not should the DGFT himself decide upon making a reference as is already the case in monopoly cases?¹²⁰ An argument against such a change of law would be that the public interest criterion against which mergers are assessed in the U.K. leaves ample room for a wide range of political considerations.¹²¹ One might argue that this requires the decisions to be taken by a politician who is answerable to Parliament rather than a public servant like the DGFT. There is, hence, a correlation between procedural and substantive law which can also be seen in comparison to Germany. In Britain, merger control has through the public interest criterion a political dimension. Consequently, the Secretary of State takes the decisions. In Germany, merger control is exclusively based on competition and by and large seen as a technical administrative matter with no role for politicians: hence, independent public servants of the Cartel Office decide.¹²² The question is, however, whether the public interest is the right criterion against which to assess mergers and whether merger control should be seen as having a political dimension. The advantages and

118 See House of Commons speeches or written answers on Merger Policy: *Lord Tebbit*, July 5, 1984; *Lord Young*, October 8, 1987; *John Redwood*, March 13, 1990; *Peter Lilley*, July 26, 1990; *Michael Heseltine*, May 13, 1992. See also *DTI*, *Blue Paper on Mergers Policy*, 1988, p. 7; *OFT*, *Mergers: A guide to the procedures under the Fair Trading Act 1973*, p. 8.

119 See Chapter 6.4.2. at pp. 254.

120 As to monopolies see sec. 50 FTA 1973.

121 See Chapter 6.4.2. at pp. 254.

122 See Chapter 7.4.1. at pp. 304 and Chapter 7.5. at pp. 315.

disadvantages of the either system will be further discussed in Chapter 7.

6.3.3. The MMC Procedure

A reference to the MMC has far reaching implications for the companies involved.¹²³ Some of these implications are immediate legal consequences,¹²⁴ most notably, a public takeover offer lapses automatically under the provisions of the City Code.¹²⁵ Equally important are the economic consequences of a reference.¹²⁶ The MMC procedure is costly and time-consuming to the parties involved.¹²⁷ Extensive submissions have to be made, hearings to be attended and enquiries to be answered, which inevitably consumes a considerable amount of top-level management time. The costs of external advisors, i.e. solicitors, accountants etc., are substantial too.¹²⁸ These expenses, together with the uncertainty that unavoidably comes with a procedure of up to six months,¹²⁹ quite often cause the parties to abandon the merger proposal voluntarily

123 Address: MMC, New Court, 48 Carey Street, London WC2A 2JT, Tel. 0171/3241467.

124 Sec. 74 FTA 1973: the Secretary of State has power to make interim orders with a view to preventing the parties from action which could impede the MMC's investigation; Sec. 75 (4A) FTA 1973: the parties are automatically prevented from further acquiring interests in each other.

125 Rule 12 (a) of the City Code stipulates that "*is must be a term of the offer that it will lapse if there is a reference before the first closing date or the date when the offer becomes or is declared unconditional as to acceptances, whichever is the later.*"

126 For a thorough economic analysis see *Franks/Harris*, Shareholder Wealth Effects of UK Takeovers: Implications for Merger Policy, p. 149, 154 et seq.

127 *Trade and Industry Committee*, Fifth Report: U.K. Policy on Monopolies, 1995, para 39. *Finbow/Parr*, U.K. Merger Control, para 5.001.

128 *Trade and Industry Committee*, Fifth Report: U.K. Policy on Monopolies, 1995, para 39.

129 As to the timing see Chapter 6.3.3.(4) at pp. 242.

once a reference has been made, as Table 12 below demonstrates.¹³⁰

Table 12: Outcome of References

Year	References made by the Secretary of State	MMC Finding against	Mergers Cleared	Merger Abandoned
1986	13	3	3	7
1987	6	3	3	-
1988	10	4	4	2
1989	15	5	8	2
1990	27	11	13	3
1991	7	3	3	1
1992	10	5	1	4
1993	2	-	2	-

Source: Dan Goyder, *Public Interest Criteria*, Fordham 1994, p. 130

(1) Function of the MMC

On a merger reference, the MMC’s duty is to investigate and report on two questions: (a) whether a merger situation qualifying for investigation has been created, and (b) if so, whether the creation of that situation operates, or may be expected to operate, against the public interest.¹³¹ The MMC has no power to initiate its own proceedings nor is it empowered to negotiate undertakings with the parties in lieu of reporting or is in any way involved in the

130 *Butterworth’s Competition Law*, Div. VII, para 347; *Finbow/Parr*, U.K. Merger Control, para 5.010.
131 Sec. 69 (1) FTA 1973.

enforcement of the action following an adverse report.¹³² The basic idea is to have an expert commission free from any conflicts of interest and independent of government assess the merger. Its role has been likened by the Chairman of the MMC, *Graeme Odgers*, to that of a jury in a criminal trial, with the OFT playing the role of prosecutor.¹³³ Only if this impartial jury is convinced that the merger is detrimental to the public interest, the merger may finally be blocked by the Secretary of State.¹³⁴ Reasonable doubt as to the merits of the merger is not enough for "a conviction" as was pointed out in *British Sugar/Berisford*.¹³⁵ This demonstrates again the liberal attitude of the Fair Trading Act towards mergers.¹³⁶ There is a basic presumption in favour of mergers in the U.K.¹³⁷

(2) Personnel and Resources

The MMC is a statutory body funded by the DTI. Its expenditure in the financial year 1994/1995 amounted to £6.8 million including £1.4 million accommodation charges.¹³⁸

The Commission is headed by a full-time chairman, who is appointed by the Secretary of State for Trade and Industry.¹³⁹ The

132 *Lipworth*, Merger Control in the U.K., Fordham 1990, p. 205, 210.

133 *Trade and Industry Committee*, Fifth Report, 1995, para 55, Q. 18.

134 Sec. 73 FTA 1973. See, however, the proposals made by *Trade and Industry Committee*, First Report, Takeovers and Mergers, 1991, para 297. Discussed below: 7.3.4.

135 *S & W Berisford Ltd. and British Sugar Corporation Ltd*, HC 241, 1980-81, para 9.40: "The question we have to consider is not merely whether there is a possibility that the merger will operate against the public interest. If only a possibility were required, hardly any merger could ever be allowed to proceed, for it is very rarely that such a possibility can be quite excluded. The question is whether the evidence creates an expectation that the merger will operate against the public interest. To put the matter colloquially, the required conclusion is not, 'This may happen', but 'We expect that this will happen'."

136 See 7.3.1.(1).

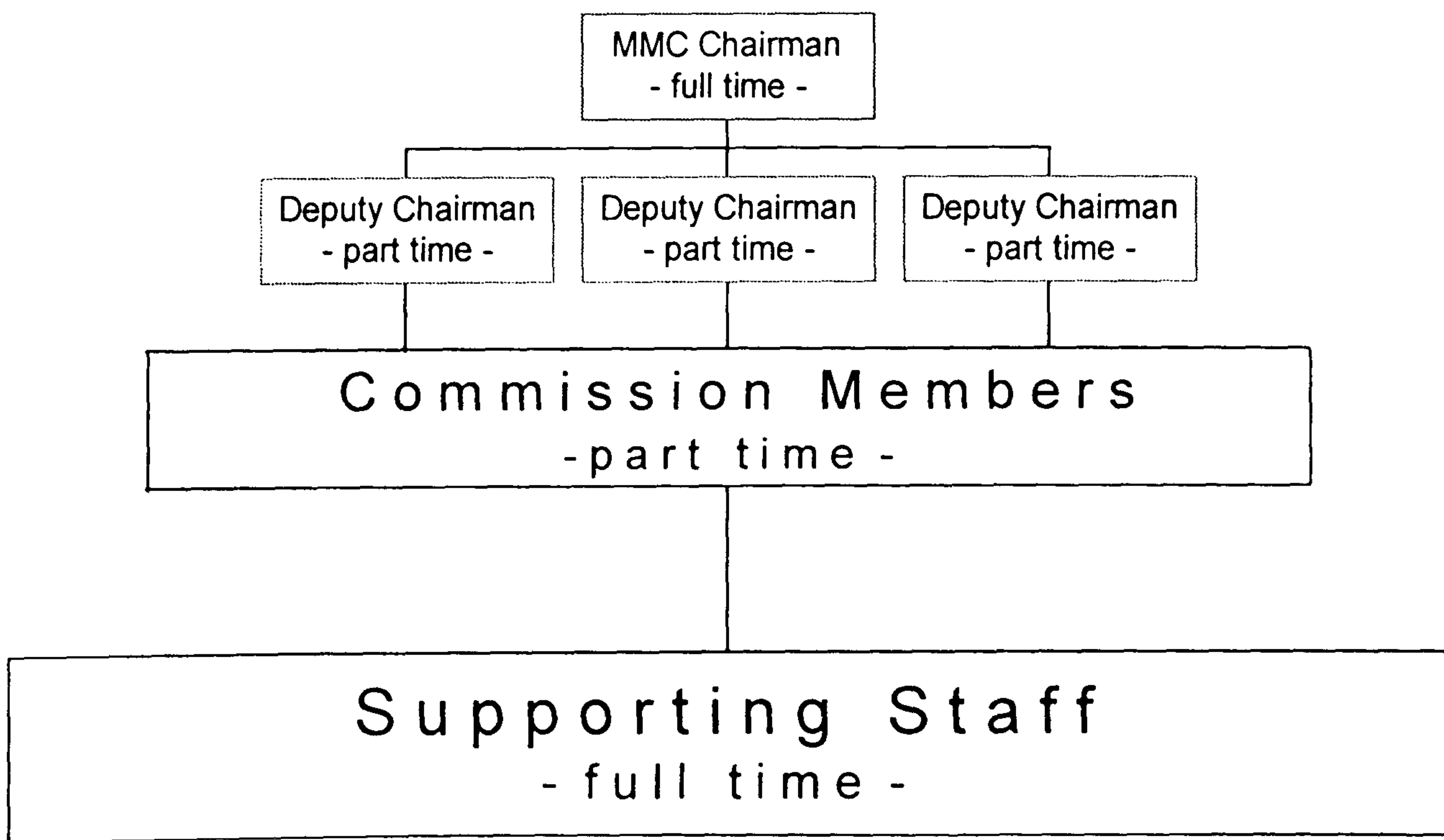
137 *Butterworth's Competition Law*, Div. VII, para 347; *Finbow/Parr*, U.K. Merger Control, para 5.015; *Whish/Sufrin*, Competition Law, p. 689.

138 MMC, Annual Review 1994, p. 11-12.

139 See Schedule 3 of the FTA 1973.

Secretary of State also appoints the three Deputy Chairmen, who work part time on a 3 1/2 days basis. The chairman selects the Members, of which at present about 31, including the three Deputy Chairman, are appointed. They are paid for 1 1/2 days a week. The Members are in their inquiries supported by the MMC's staff, comprising about 80 officials, of which about two-thirds are direct staff of the MMC and the remainder are on loan from other government departments, most notably the DTI.¹⁴⁰

Once a reference has been made, the Chairman appoints a specific group comprising usually five or six Members headed by a Chairman to investigate and report on the merger.¹⁴¹ This group is supported by a team of staff, including inter alia economic advisers, accountants, industrial, and legal advisers. The Members take the final decision as to the public interest question.¹⁴² The following chart sets out the basic organisational structure of the MMC.



140 For brief biographies of the MMC members and further details regarding the staffing refer to the MMC's Annual Review 1994.

141 See MMC, Fact Sheets 1 and 4.

142 Reg. 16 of Schedule 3 of the FTA 1973.

The part-time nature of the MMC differs completely from the structure of the German Cartel Office where full-time public servants have the exclusive responsibility for the investigation and decision-taking.¹⁴³ The part-time nature of the MMC has both strengths and weaknesses. On the one hand the MMC is on a part-time basis able to attract top people with different backgrounds in industry, business, the professions etc as the impressive biographical list of commissioners included in the Annual Reports of the MMC clearly demonstrates.¹⁴⁴ These high calibre people are likely to be capable of making valuable contributions which career-officials who have never ever worked outside the public sector and do therefore not have the industry experience MMC members have, could probably not make in the same way. However, a certain risk inherent in the British secondment policy is that of conflict of interest in the person of individual members. It is interesting to note that the German legislator in specifically ruling out secondments of directors from private companies to the Federal Cartel Office has taken a view diametrically opposed to the British one.¹⁴⁵ The U.K.-style co-operation between public and private sector by way of secondments is unknown in Germany.

Furthermore, the question has been raised of how serious a one-day-per-week commitment really can be.¹⁴⁶ Moreover, during the periods when the Commissioners are not actually part of a group investigating a merger, they are not involved with the MMC at all. The point has been made by a number of witnesses to the Trade and Industry Committee that the Commission members are no

143 Sec. 48 V GWB (incompatibility) even prohibits the Cartel Office staff from having any outside interests in the private sector in order to safeguard their independence! See Chapter 7.4.1.(3) at pp. 307.

144 MMC, Annual Review 1994, p. 7-9.

145 Sec. 48 V GWB.

146 Trade and Industry Committee, Fifth Report, 1995, para 56.

experts on competition matters and that they are not always as well-briefed as the parties wished.¹⁴⁷ It has also been alleged that because of the only sporadic involvement of the individual Commissioners they are prone to be dominated by particular group members with strong personalities and/or special knowledge, as, by the way, is often the case with "real" juries too.

On the basis of diverse evidence the 1995 Trade and Industry Committee came to the conclusion that *"there is a general dissatisfaction among industry and consumers with the present arrangements"* which led to the recommendation *"that appointments to the MMC be made on a full-time basis and that encouragement be given to secondment from industry, academia, consumers' groups and trade unions."*¹⁴⁸ A system as proposed by the Committee would steer a middle course combining the strengths of the British and German systems while to some extent avoiding their respective detriments.

147 *Trade and Industry Committee, Fifth Report, 1995, para 67*

148 *Trade and Industry Committee, Fifth Report, 1995, para 62. This was already recommended by the 1991 Trade and Industry Committee Report on Takeovers and Mergers, para 126.*

Table 13: Background of MMC Members

	1988	1989	1990	1991	1992	1993	1994
Economics	3	3	6	8	8	8	7
Accountancy	6	6	5	4	3	2	2
Law	4	7	8	9	8	8	7
Business	15	12	16	14	15	12	12
Finance	7	6	6	4	4	4	3
Other ¹⁴⁹	8	8	9	7	9	8	7

Source: MMC evidence to the Trade and Industry Committee, 5th Report, 1995.

(3) Policy of the MMC

The key provision guiding the MMC - and, indeed, the whole British merger control system - is section 84 (1) of the FTA 1973 which reads as follows:

149 Includes Trades Union, consumer, civil service backgrounds.

84. (1) *In determining for any purposes to which this section applies whether any particular matter operates, or may be expected to operate, against the public interest, the Commission shall take into account all matters which appear to them in the particular circumstances to be relevant and, among other things, shall have regard to the desirability -*

(a) of maintaining and promoting effective competition between persons supplying goods and services in the United Kingdom;

(b) of promoting the interests of consumers, purchasers and other users of goods and services in the United Kingdom in respect of the prices charged for them and in respect of their quality and the variety of goods and services supplied;

(c) of promoting, through competition, the reduction of costs and the development and use of new techniques and new products, and of facilitating the entry of new competitors into existing markets;

(d) of maintaining and promoting the balanced distribution of industry and employment in the United Kingdom; and

(e) of maintaining and promoting competitive activity in markets outside the United Kingdom on the part of producers of goods, and of suppliers of goods and services, in the United Kingdom.

Unlike the OFT recommendation and the Secretary of State's reference decision, both of which are characterized by a relative lack of transparency,¹⁵⁰ the MMC stage of the procedure is transparent, since the highly detailed reports published by the MMC set out the underlying reasons for its finding in great detail. The criteria applied by the MMC in assessing the public interest will be examined in Chapter 6.4. in connection with the substantive law of merger control.

Suffice it to say at this stage that it is widely acknowledged that the MMC has for various reasons no, or at least no dominant, role in formulating British merger policy.¹⁵¹ One obvious reason is that the MMC is not empowered to initiate its own investigations. It only gets what the Secretary of State wants it to have, and it is the Secretary of State who finally takes the decision upon an adverse finding. Furthermore, there is no system of precedent. This last point has led to the reproach of inconsistency and unpredictability on the part of the MMC.¹⁵² The MMC argues, however, that each case needs to be considered on its own merits and that an inflexible policy in assessing the public interest would be contrary to the companies' interests who would not welcome a dependence on past cases.¹⁵³ The MMC has a point in so far as merger cases do very much depend on factual matters, i.e. on an evaluation and prognostication of the development of the relevant markets after the merger has taken place, unlike judicial decisions which tend to be based to a much larger extent on purely legal questions. The system of precedent which works for the judiciary, and upon which common law is in fact based, is not as easily transferable to merger control as it might seem. However, in response to the criticism of unpredictability, the MMC has published a small booklet setting out in a simple and clear way the basics of competition assessment.¹⁵⁴ A more technical barrier to formulating a consistent merger policy lies in the organisational structure of the MMC. As the investigations are undertaken by groups of commissioners who work part-time on an ad-hoc basis on individual merger cases and are unlike, for example, the officials of the German Federal Cartel Office not permanently involved in the merger control process there clearly is a practical

151 *Whish/Sufrin*, Competition Law, p. 689; *Trade and Industry Committee*, Fifth Report, 1995, para 46.

152 See the evidence given to the *Trade and Industry Committee*, Fifth Report, 1995, para 44. Also *Raybould/Firth*, Comparative Law of Monopolies, Pt. II, 4.4.1, p. 450.

153 *Finbow/Parr*, U.K. Merger Control, para 5.016; *Trade and Industry Committee*, Fifth Report, 1995, para 46.

154 *MMC*, Assessing Competition, 1993.

difficulty in developing a coherent merger policy. The point is that given the current structure of the merger control process in Britain, the MMC, designed as a "jury", is not enabled to formulate a merger policy of its own, and therefore, this should not be expected of it.¹⁵⁵ The problem of inconsistency, inherent in the present structure, can only properly be addressed through an organic reform of the MMC's role.

(4) Timing

The merger reference by the Secretary of State has to specify a period, which must principally not exceed six months, within which the report on the reference is to be made.¹⁵⁶ In practice, since the publication of the Blue Paper on Mergers Policy in 1988,¹⁵⁷ the internal MMC procedure has been streamlined considerably and the Secretary of State nowadays usually only allows a three months period. As a thorough investigation inescapably takes some time, there appears, looking at the internal proceedings of the MMC, to be little scope for further streamlining of the process.¹⁵⁸

6.3.4. The Secretary of State's Action following the Report

If there has not been an adverse finding by the MMC, the merger is automatically cleared. The Secretary of State has no further role to play. Hence, in this case the final decision is taken by the MMC!

155 *Trade and Industry Committee*, Fifth Report, 1995, para 56.

156 Sec. 70 (1) FTA 1973. For an exception to this rule see sec. 70 (2).

157 DTI, Blue Paper on Mergers Policy, HMSO 1988.

158 *Finbow/Parr*, U.K. Merger Control, paras 5.004 and 10.005.

In the event of an adverse MMC finding the Secretary of State is empowered to take the final decision - which usually takes another couple of weeks.¹⁵⁹ During this period he considers what action to take in the light of the MMC's conclusions and whether to make excisions from the published version of the MMC report. He may by way of orders, which are set out in detail in Part I and II of Schedule 8 to the Fair Trading Act, either block the merger or attach conditions to it. He may also clear the merger unconditionally, although it is rather rare in practice that the Secretary of State deviates materially from the MMC's recommendations. In practice the route most often taken by the Secretary of State is to ask the DGFT to enter into negotiations with the merging parties in order to remedy the adverse effects specified in the MMC report by way of binding undertakings in lieu of orders.¹⁶⁰

Whatever course is taken following an adverse report, the Secretary of State is obliged under section 73 (3) of the Fair Trading Act to *"take into account any recommendations included in the report of the Commission and any advice given by the Director ..."* However, as was made clear by Lord Justice Dunn in *R. v. Secretary of State, ex parte Anderson Strathclyde plc*, this provision does in no way fetter the Secretary's options: *"the Act read as a whole shows that the Secretary of State is not bound by the conclusions of the majority of the commission, that he has a wide discretion in deciding whether to make any order at all, in exercising that discretion he is entitled to take into account all the relevant circumstances, and to consider the opinion of the minority of the commission, and also representations and advice from persons other than members of the commission."*¹⁶¹ Once again, these representations confirm the

159 DTI, Blue Paper on Mergers Policy, para 5.12; Lipworth, Merger Control in the U.K., Fordham 1990, p. 205, 207; Critical to the length of that period *Finbow/Parr*, U.K. Merger Control, paras 7.005 and 10.006.

160 A thorough analysis of this topic provide *Finbow/Parr*, U.K. Merger Control, para 7.011 et seq.

161 *R. v. Secretary of State for Trade and others, ex parte Anderson Strathclyde plc* [1983] 2 All ER 233, 242.

overall impression that merger control in Britain is a highly discretionary affair.

Interestingly, the Trade and Industry Committee recommended in its 1991 report on Takeovers and Mergers to extend the Secretary of State's powers to block a merger to the case where the MMC has cleared it.¹⁶² The argument put forward is that the final decision should in any event be taken by the Secretary of State as he is answerable to Parliament, which the MMC is not.

From a dogmatic point of view this seems consistent and in line with the general role of the MMC as an advisory body and the role of the Secretary of State as the ultimately responsible decision-taker. However, the law as it stand reflects the liberal attitude towards mergers taken by the Fair Trading Act in the sense of a basic presumption in favour of mergers. To extend the Secretary of State's power to cases where the MMC has cleared the transaction would free the Secretary of State entirely from the MMC's findings. The Secretary of State already enjoys completely unfettered discretion when making the reference decision.¹⁶³ To give him even more power would - rightly or wrongly - further increase the impression that merger decisions might be influenced by political considerations and, thus, contribute to the uncertainty felt by the industry because of the already wide discretion. From a European and German perspective, where merger decisions are - at least in theory - seen as administrative, and not political, decisions, an extension of the Secretary of State's power would further increase the gap between the regulatory systems.

162 *Trade and Industry Committee, First Report, Takeovers and Mergers, 1991, para 297.*

163 See Chapter 6.3.2. at pp. 229.

6.4. The Substantive Appraisal Criteria

It has been pointed out earlier that merger control in the U.K. is based on the broad concept of public interest.¹⁶⁴ Section 84 of the Fair Trading Act 1973 stipulates that the MMC, in deciding whether or not a merger may be expected to operate against the public interest, shall take into account “*all matters which appear to them in the particular circumstances to be relevant ...*” It is clear from the wording of section 84 that the MMC enjoys comprehensive discretion. Given this wide discretion it is not surprising that no application for judicial review¹⁶⁵ of a decision made under the merger provisions has ever been successful in the United Kingdom.¹⁶⁶ The judicial self-restraint exercised by the courts and the underlying reasons for this are comparable to the situation under the City Code, where also no application for judicial review has been successful so far.¹⁶⁷

The objective of this chapter is to examine the criteria applied by the MMC in assessing the effects of a merger on the public interest.

164 See Chapter 6.3.3.(3) at pp. 239.

165 R v. Monopolies and Mergers Commission, ex parte Argyll Group plc, [1986] 2 All ER 257; R v. Monopolies and Mergers Commission, ex parte Elders IXL, [1987] 1 All ER 451; R v. Monopolies and Mergers Commission, ex parte Matthew Brown plc, [1987] 1 All ER 463; R v. Monopolies and Mergers Commission, ex parte Air Europe, [1988] 4 BCC 182; R v. Monopolies and Mergers Commission, ex parte Argyll Group plc, [1986] 2 All ER 257.

See also R v. Secretary of State, ex parte Anderson Strathclyde plc [1983] 2 All ER 233 (discussed: Chapter 6.3.4.) and Lonrho plc v. Secretary of State, [1989] 2 All ER 609 (discussed: Chapter 6.3.2.).

166 For details see *Hornsby*, Judicial Review of Decisions of the UK Competition Authorities: Is the Applicant Bound to Fail? [1993] 5 ECLR 183 et seq; *Finbow/Parr*, U.K. Merger Control, 9.019; *Whish/Sufrin*, Competition Law, p. 700.

167 See Chapter 3.1.2.(4) at pp. 51.

6.4.1. Competition

In practice, the single most important issue in assessing mergers is competition. The underlying question is whether the merger is likely to confer market power which the new enterprise may be able to exploit at the expense of U.K. customers and consumers.¹⁶⁸ The emphasis on competition originates in the Fair Trading Act itself which mentions the promotion of competition in section 84 (1)(a), (c), and (e).¹⁶⁹ Competition has been given further weight as it has been consistent government policy¹⁷⁰ to focus mainly on competition since the so called “Tebbit Doctrine” was pronounced in 1984: *“References to the MMC would be made primarily, but not exclusively, on competition grounds, taking into account the international dimension of competition.”*¹⁷¹ Since 1984, references based solely on non-competition grounds have been very rare.¹⁷²

Assessing the potential effect of a merger on competition is inherently difficult. The DTI Blue Paper on Mergers Policy put it this way: *“It is not possible to set out rules of thumb which can be straightforwardly or mechanically applied to all cases: there is an irreducible element of judgement involved in assessing the likely effects of a merger on competition, which cannot be captured in formulae or statistics, and flexibility is essential in dealing with the unique circumstances of each case.”*¹⁷³ However, there are a

168 DTI, Blue Paper on Mergers Policy, para 2.18.

169 See the exact wording of sec. 84 set out in full in Chapter 6.3.3.(3) at pp. 239.

170 See House of Commons speeches or written answers on Merger Policy: Lord Tebbit, July 5, 1984; Lord Young, October 8, 1987; John Redwood, March 13, 1990; Peter Lilley, July 26, 1990; Michael Heseltine, May 13, 1992. See also DTI, Blue Paper on Mergers Policy, 1988, para 2.14 et seq; OFT, Mergers: A guide to the procedures under the Fair Trading Act 1973, p. 8; MMC, Assessing Competition, para 7. For an evaluation see also Butterworth's Competition Law, Div. VII, paras 146 et seq.

171 House of Commons written answer, July 5, 1984.

172 DTI, Mergers Policy, para 2.27; Soames, Merger Policy: As Clear as Mud?, [1991] 2 ECLR 53, 56. See also Chapter 6.4.2. at pp. 254.

173 DTI, Blue Paper on Mergers Policy, para 2.15.

number of key factors commonly applied by the MMC, most notably, but not exclusively:¹⁷⁴

- (1) Market share
- (2) Remaining competitors
- (3) Countervailing bargaining power
- (4) Barriers to entry and expansion

(1) Market Share

As one would expect, the market share of the new enterprise plays an important role where a horizontal merger is concerned.¹⁷⁵ Horizontal mergers are mergers between actual competitors.¹⁷⁶ The market share depends, of course, on how the relevant product and geographic market is defined.¹⁷⁷ The economic criteria applied in indentifying the relevant market cannot be discussed in detail here. Suffice it to say that the demand substitutability test plays a dominant role with regard to the relevant product market, whereas issues like transport costs and the perishability of the products in question have some bearing on the definition of the relevant geographic market.¹⁷⁸ However, as the MMC put it: “*There is no*

174 MMC, Assessing Competition, paras 9, 12-24. *DTI*, Blue Paper, para 2.18.

175 *OFT*, Mergers: A guide to the procedures under the FTA 1973, p. 10-11; *OFT*, Mergers: The Content of Submissions, para 12; *OFT* Research Paper 1, Market Definition in U.K. Competition Policy, 1993.

176 References of vertical or conglomerate mergers are rare as detrimental effects are far more difficult to determine as competition issues do not arise by definition. See *Raybould/Firth*, Comparative Law of Monopolies, 4.4.2., p. 458 et seq; *Finbow/Parr*, U.K. Merger Control, paras 6.044 and 6.047.

177 Examples of rather narrowly defined markets provides *Soames*, Merger Policy: As Clear as Mud?, [1991] 2 ECLR 53, 59.

178 For an analysis of the factors relevant in identifying the relevant markets see *OFT*, Mergers: A guide to the procedures of the FTA 1973, p. 9; *Soames*, Merger Policy: As Clear as Mud?, [1991] 2 ECLR 53, 55; *Finbow/Parr*, U.K. Merger Control, para 6.017 and 6.005 et seq.

*simple solution and there can be no hard and fast rules on how to define the market.*¹⁷⁹

The market share of the new enterprise is, however, not the only, and in many cases not even the decisive, factor as the *Gillette/Parker* and *Kingfisher/Dixons* cases illustrate:¹⁸⁰

(a) ***Gillette/Parker***:¹⁸¹ When *Parker Pen Holdings Ltd* was acquired by *Gillette*, which owned *Paper Mate* and *Watermann*, *Gillette's* market share in the supply of refillable writing instruments increased from some 7 per cent to about 60 per cent in value. In view of the fact, however, that there were about 40 other competing brands of refillables supplied to the U.K. market, the MMC cleared the merger.

(b) ***Kingfisher/Dixons***:¹⁸² In the *Kingfisher/Dixons* case competition in the market for electrical appliances was concerned. The bidder, *Kingfisher*, had through its subsidiary *Comet* a market share of about 9 per cent whilst *Dixons* had a 17 per cent share. The takeover would consequently have resulted in only a 26 per cent market share for *Kingfisher*. It was nevertheless blocked by the MMC. This decision was taken on the grounds that *Comet* (*Kingfisher*) and *Dixons* were competing vigorously on a national level and that retail prices for electrical appliances were likely to rise if the rivalry between *Comet* (*Kingfisher*) and *Dixons* were to disappear.

These cases demonstrate the limited significance of the market share taken separately: a merger leading to a market share of 60 per cent was given the green light, whereas a takeover resulting in only a 26 per cent market share was blocked on competition grounds.¹⁸³

179 MMC, Assessing Competition, para 16.

180 *Finbow/Parr*, U.K. Merger Control, para 6.017 and 6.020.

181 The *Gillette* Company and *Parker Pen Holdings Limited*, 1993, Cm 2221.

182 *Kingfisher plc* and *Dixons Group plc*, 1990, Cm 1079.

183 For recent examples see also: *Avenir Havas Media SA* and *Brunton Curtis Outdoor Advertising Ltd*, 1991, Cm 1772: adverse finding (25.2 per cent); *Elders IXL Ltd* and *Grand Metropolitan*, 1990, Cm 1227: adverse

(2) Remaining Competitors

The strength of remaining competitors, or more generally the structure of the market, is another factor which is regularly considered by the MMC. In this context, the MMC has, *inter alia*, regard to the number, size and market shares of competitors, international trade and openness of the market, the nature of competition (i.e. based on price, quality, or after-sales service etc), the financial resources of the competitors, and the rate of growth of the market.¹⁸⁴

It has been claimed that the MMC takes too parochial and insular an approach when it comes to giving appropriate weight to the likely effect of imports on U.K. competition.¹⁸⁵ However, it appears doubtful whether this criticism is justified. At least since the “Tebbit Doctrine” in 1984, which promised to take “*into account the international dimension of competition*”,¹⁸⁶ the government has been fully aware of the issue of import penetration. This is documented in various official publications¹⁸⁷ and MMC reports.¹⁸⁸ A different

finding (20 per cent); Hillsdown Holdings Plc and Associated British Foods Plc, 1992, Cm 2004: cleared (80-90 per cent).

184 MMC, *Assessing Competition*, para 13.

185 Reported by the DTI, *Blue Paper on Mergers Policy*, para 2.5 and Soames, *Merger Policy: As Clear as Mud?*, [1991] 2 ECLR 53, 57; Whish/Sufrin, *Competition Law*, p. 696.

186 House of Commons written answer, July 5, 1984.

187 See the following official documents: DTI, *Blue Paper on Mergers Policy*, para 2.5; OFT, *Mergers: a guide to the procedures under the FTA 1973*, p. 11; MMC, *Assessing Competition*, para 13 (b): “*The intensity of competition in a market is likely to be affected by the degree of its openness to international trade. Barriers to imports, including legal or institutional barriers (both tariff and non-tariff), transport costs and cultural barriers such as preferences for nationally-manufactured products, may to some extent isolate domestic producers from international competition. Although import penetration is relevant in assessing the intensity of competition, the source of the imports needs to be considered since import figures may overstate the intensity of competition. For example, imports may come from foreign subsidiaries within the same international group as domestic firms, may be aimed at particular sectors of the*

matter is, though, whether a national competition authority is really able to assess market events going on abroad correctly. It appears that for factual reasons the insight into foreign markets is necessarily limited. How, for example, can the British or German merger control authorities know how some South-Korean or Taiwanese actual or potential competitor is going to respond to a national British or German merger, whether they enter the market or not?

(3) Countervailing Bargaining Power

Another factor which the MMC has frequently taken into account in assessing competition is that of countervailing bargaining power of either suppliers or customers of the newly merged enterprise.¹⁸⁹ Where its suppliers or buyers are in a particularly strong position, the merged enterprise is likely to be unable to exploit its market position even if it enjoys a comfortable market share. Countervailing bargaining power on the part of a supplier is likely to exist where the merged enterprise depends upon the supplier's products and cannot switch to alternative suppliers easily. Countervailing bargaining power on the part of a buyer may exist where the buyer purchases a

market, or may be regarded by some consumers as an unreliable source of supply."

188 See e.g. Monsanto Company and Rhône-Poulenc SA, 1989, Cm 826, para 1.5: *"We have found that Rhône-Poulenc's ability to exploit its predominant position in the supply of salicylic acid.... would be constrained by competition, particularly from Eastern European and Third World sources. We believe that as a result Rhône-Poulenc would be unlikely to be able to impose unreasonable price increases. We accordingly unanimously conclude that the proposed merger may be expected not to operate against the public interest."*; BICC Plc and Sterling Greengate Cable Company Ltd, 1990, Cm 1131, para 6.41; Trelleborg AB and McKechnie Extruded Products Ltd, 1990, Cm 1384, para 1.4; Sara Lee Corporation and Reckitt & Colman Plc, 1992, Cm 2040, para 6.32. The General Electric Company plc, Siemens AG and The Plessey Company plc, 1989, Cm 676, para 1.7.: *"Furthermore, there have been changes in the economic environment of the United Kingdom since 1986, with greater emphasis on the development of a more open European market and international collaboration in defence."*

189 MMC, Assessing Competition, para 18-20.

large portion of the merged enterprises' production.

An example of the MMC's approach can be found in *Hillsdown Holdings/Associated British Food (Anglia)* where following the merger *Hillsdown's* market share accounted for over 50 per cent in the market for canned seasonal vegetables and was even higher in the market for canned fruits. In assessing the impact on competition the MMC concluded: "*There are now only five canners of seasonal fruit and vegetables in the United Kingdom and new entry is unlikely. Hillsdown's ability to exploit its high market share is nevertheless limited by a number of factors. The buying power of the multiple retailers is large and their bargaining power is increased by their proportion of high-volume own-label sales. None of Hillsdown's major customers*¹⁹⁰ *objected to the merger situation and most were unconcerned by the change.*"¹⁹¹ The merger was cleared.

(4) Barriers to Entry and Expansion

It is an elementary interrelationship in a functioning market that where an enterprise becomes too powerful and exploits its market position by way of rising prices above the competitive level new competitors are likely to enter the market to offer the product or service at a lower price. Hence, the threat of entry of new competitors deters existing firms to some extent from abusing their market power even where they enjoy relatively high market shares. This important constraint upon the exercise of market power by incumbents does, however, not work where serious (artificial) barriers to new entry exist.¹⁹² Where such barriers exist, incumbents

190 Companies like Tesco and Sainsbury.

191 Hillsdown Holdings PLC and enterprises belonging to Associated British Foods PLC, 1992, Cm 2004, para 1.5.

192 Sec. 84 (1)(e) FTA 1973 therefore requires the MMC to "have regard to the desirability ... of facilitating the entry of new competitors into existing

may raise prices above the competitive level without actually inducing new competitors: the market is to the disadvantage of customers and consumers artificially constrained.¹⁹³

What constitutes a barrier to entry has been the subject of heated debate among economists, most notably between the *Chicago School*, favouring a very narrow definition according to which only government policy and regulation could be regarded as barriers, and the prevailing *Harvard School*, advocating a much broader approach.¹⁹⁴ On the basis of its reports¹⁹⁵ there is no doubt that the MMC in practice champions the *Harvard* approach.¹⁹⁶ In its booklet "Assessing Competition" the MMC identifies the following factors as potential barriers to entry:

- (a) *Limited supplies* (of raw materials or facilities, or lack of access to appropriate technology).
- (b) *Institutional or regulatory barriers* (licensing requirements, safety or quality standards, planning permissions, intellectual property rights, disposal or pollution controls).

markets." Stressing the importance of entry barriers, Littlechild, *Myths and Merger Policy*, p. 301, 313 et seq.

193 See MMC, *Assessing Competition*, para 21; OFT, *Barriers to Entry and Exit in UK Competition Policy*; *Finbow/Parr*, U.K. Merger Control, para 6.030-6.038; *Harbord*, *The Analysis of Barriers to Entry*, [1995] 5 ECLR 319 et seq.; Soames, *Merger Policy: As Clear as Mud?*, [1991] 2 ECLR 53, 61;

194 See *Harbord*, *The Analysis of Barriers to Entry*, [1995] 5 ECLR 319, 320 with further references.

195 See e.g. Thomson Travel Group and Horizon Travel Ltd, 1989, Cm 554; Kingfisher plc and Dixons Group plc, 1990, Cm 1079; British Airways plc and Sabena SA, 1990, Cm 1155; Sligos SA and Signet Ltd, 1991, Cm 1450; Prosper De Mulder Ltd and Croda International, 1991, Cm 1611; Avenir Havas Media SA and Brunton Curtis Outdoor Advertising Ltd, 1991, Cm 1737; Bond Helicopters Ltd and British International Helicopters Ltd, 1992, Cm 2060; *Gillette Company and Parker Pen Holdings Limited*, 1993, Cm 2221.

196 Also *Harbord*, *The Analysis of Barriers to Entry*, [1995] 5 ECLR 319, 321; *Finbow/Parr*, U.K. Merger Control, para 6.030.

- (c) *Economies of scale* (due to the market structure the entrant has to come in on a large scale if he is to operate profitably).
- (d) *Economies of scope* (there are joint costs which make entry profitable only if the entrant competes in two or more product markets at the same time).
- (e) *Economies of vertical integration* (in vertically integrated industries it may be difficult to gain access to supplies or distribution channels because of exclusive supplying or dealing arrangements).
- (f) *Sunk costs* (i.e. costs which are not recoverable on market exit, e.g. advertising, research and development, specialised machinery, fees for licences and permissions etc.)
- (g) *Excess capacity by incumbents* (this may enable an incumbent to retaliate forcefully upon entry of a new competitor, e.g. by lowering prices).
- (h) *Product differentiation and brand loyalty* (it may be difficult or involve huge advertising costs for a new entrant to match the strong brand image of an incumbent).¹⁹⁷

It would go beyond the scope of this work to discuss each of these economic factors in detail. One example may suffice to demonstrate how such barriers are taken into consideration by the MMC:

When *Bond Helicopters Ltd* bid for the North Sea helicopter business (transport of personnel to and from the oil and gas fields) of *British International Helicopters Ltd (BIH)*, the result of the proposed

197 See for a detailed analysis *Parr/Hughes*, *The Relevance of Consumer Brands and Advertising in Competition Inquiries*, [1993] 4 ECLR 119 et seq.

merger would have been that only two competitors would have remained in the North Sea helicopter market, namely *Bond* and a third firm, *Bristow*, each of which approximately having a 50 per cent market share.¹⁹⁸ Assessing the likely impact on competition, the MMC argued that any potential new entrant would face tough conditions, so that the emergence of a new competitor was not on the cards: *"A new entrant needs finance, a proven safety record and aircraft and staff that meet stringent safety requirements. He is likely to face difficulty in finding suitable bases.... We concluded that without promise of firm contracts from customers, successful entry on a scale likely to provide effective competition was unlikely within a reasonable period.... We therefore conclude that if the acquisition takes place competition will be reduced and prices may be expected to rise."*¹⁹⁹ The merger was blocked.

To sum up, after defining the relevant market and assessing the immediate loss of competition resulting from the merger, the MMC focuses on the question whether there are potential competitors in related markets that could quickly and easily enter or expand into the market in question should following the merger prices increase. In assessing competition, the ease of entry for potential competitors is therefore almost as important as the market share criterion itself.²⁰⁰

6.4.2. Public Interest Issues other than Competition

Over the years, the MMC has found a wide range of different

198 Bond Helicopters Ltd and British International Helicopters Ltd, 1992, Cm 2060. The merger would have increased Bond's market share from 29 per cent to 49 per cent.

199 Bond Helicopters Ltd and British International Helicopters Ltd, 1992, Cm 2060, paras 1,6 and 1.8.

200 *OFT, Mergers: A guide to the procedures under the FTA 1973*, p. 11; *Harbord, The Analysis of Barriers to Entry*, [1995] 5 ECLR 319, 322.

factors other than competition to be operating against the public interest,²⁰¹ for example:

- the creation of regional unemployment,²⁰²
- the loss of research and development capacity,²⁰³
- leveraged financing techniques,²⁰⁴
- foreign ownership and reciprocity,²⁰⁵
- foreign state control,²⁰⁶
- national security,²⁰⁷
- the past industrial relations record of the bidder, and²⁰⁸
- incompatibility of the respective managements.²⁰⁹

201 For a brief discussion of those issues see also the *DTI Blue Paper on Mergers Policy*, para 2.20-2.28.

202 H Weidmann AG and B S & W Whiteley Ltd, 1975, Cmnd 6208, para 115 (cleared); The Sunlight Service Group Plc and Johnson Group Cleaners Plc and Initial Plc and Johnson Group Cleaners Plc, 1983, Cmnd 8868; The Hongkong and Shanghai Banking Corporation, Standard Chartered Bank Ltd and The Royal Bank of Scotland Group Ltd, 1982, Cmnd 8472; Enserch Corporation and Davy Corporation Ltd, 1981, Cmnd 8360, para 9.25: "*We foresee detriments to exports and employment arising from the loss of Davy's national character as a British bidder in overseas markets, the lengthening of the chain of management command, and the effects of certain United States legislation.*"; Charter Consolidated plc and Anderson Strathclyde plc, 1982, Cmnd 8771, para 9.20: "*We also conclude that both because it would affect employment within Anderson Strathclyde and because it would detract from the dynamism of business in the region, it may be expected to have an adverse effect upon employment in a relatively depressed part of the United Kingdom.*" As to the regional effects of a takeover on Scotland see The Hongkong and Shanghai Banking Corporation, Standard Chartered Bank Limited, The Royal Bank of Scotland Group Ltd, 1992, Cmnd 8472, para 12.7-12.19.

203 The General Electric Company and The Plessey Company Plc, 1986, Cmnd 9867; The General Electric Company plc, Siemens AG and The Plessey Company plc, 1989, Cm 676.

204 See below Chapter 6.4.2. (1) at pp. 256.

205 See below Chapter 6.4.2. (2) at pp. 258.

206 See below Chapter 6.4.2. (2) at pp. 258.

207 The General Electric Company plc, Siemens AG and The Plessey Company plc, 1989, Cm 676, para 1.9: "*... having regard to the fact that Siemens is not a United Kingdom-owned company, potential conflicts with national security requirements*" may arise.

208 Charter Consolidated Plc and Anderson Strathclyde Plc, 1982, Cmnd 8771.

209 Babcock & Wilcox Ltd and Herber Morris Ltd, 1977, HC 1975, 1976-77. For more details on this issue see *Whish/Sufrin*, Competition Law, p. 699.

However, despite occasional calls for a broader approach,²¹⁰ the emphasis has very much been on competition, at least since the pronouncement of the Tebbit Doctrine in 1984.²¹¹ Non-competition factors have not normally played a decisive role. Where they were taken into consideration they only had an exacerbating effect as an additional argument beside competition concerns.²¹²

In its Blue Paper on Mergers Policy the DTI stated: *"the Government recognise that a very small number of exceptional cases may raise a variety of public interest issues, other than competition, which it would be wrong to leave entirely in private hands. It is therefore intended to retain the open-ended public interest criterion.... But this option will continue to be used sparingly."*²¹³

It appears that since 1984 non-competition references have only been made where highly leveraged bids or foreign takeovers, in particular involving foreign state-controlled companies, were concerned.²¹⁴ Only these two issues are therefore discussed in more detail below.

(1) Leveraged Financing Techniques

There have been three references involving leveraging aspects, two of which were subsequently abandoned and only one resulted in

210 See e.g. *Trade and Industry Committee, First Report, Takeovers and Mergers*, 1991, paras 234, 249 et seq.

211 See Chapter 6.4.1. at pp. 246.

212 DTI, Blue Paper on Mergers Policy, paras 2.22 et seq; *Butterworth's Competition Law*, Div. VII, para 164; *Finbow/Parr*, U.K. Merger Control, para 4.011; *Soames*, Merger Policy: As Clear as Mud?, [1991] 2 ECLR 53, 61; *Whish/Sufrin*, Competition Law, p. 700.

213 DTI, Blue Paper on Mergers Policy, para 2.27.

214 *Trade and Industry Committee, First Report, Takeovers and Mergers*, 1991, para 236.

an MMC report:²¹⁵ the bid by *Elders IXL* for *Allied-Lyons* in 1985.²¹⁶ Highly leveraged bids, as they are commonplace in the United States, are characterized by the bidder borrowing large sums of money, sometimes by way of so-called junk-bonds, to acquire the target company, which is then broken up and sold off in order to repay the debt ("asset-stripping"). In Britain, leveraging practices are by far not as extreme as in the U.S. The City Code on Takeovers and Mergers requires bidders to provide in the offer document a detailed description of how the offer is to be financed which might have a constraining influence on bidders.²¹⁷ In particular, the City Code states: "*Where the offeror intends that the payment of interest on, repayment of or security for any liability (contingent or otherwise) will depend to any significant extent on the business of the offeree company, a description of the arrangements contemplated will be required.*"²¹⁸

The government's attitude towards leveraged bids is remarkably liberal and only very extreme cases will cause a reference, as the following quote from the DTI Blue Paper on Mergers Policy demonstrates: "*... where there are profitable opportunities arising from leveraged takeovers followed by break up of the target company, the presumption must be that the profit arises from the assets concerned being put to more efficient and more profitable use than in the original target company, and that this is to the benefit of the economy as a whole. Therefore the Secretary of State will not normally regard high leveraging on its own as a ground for reference*"²¹⁹

215 Reported by *Finbow/Parr*, U.K. Merger Control, para 4.010. and Soames, Merger Policy: As Clear as Mud?, [1991] 2 ECLR 53, 62.

216 *Elders IXL Ltd and Allied-Lyons plc*, 1986, Cmnd 9892.

217 Rule 24.2 (d) and 24.7 of the City Code.

218 Rule 24.2 (d) of the City Code.

219 DTI, Blue Paper on Mergers Policy, para 2.25.

(2) Foreign Ownership

At least since the mid 1980s it has been a consistent feature of British merger policy to welcome foreign investment regardless of whether it is made by way of acquisitions of existing companies or direct inward investment.²²⁰ Consequently, foreign ownership has not been a ground for reference in its own right, although the issue was considered a number of times²²¹ and even the DTI Blue Paper on Mergers Policy states that *"one consideration that may be relevant in some cases is the extent to which U.K. companies have reciprocal freedom to acquire companies based in the home country of the prospective acquirer."*²²² The issue of reciprocity hit the headlines when the swiss company *Nestlé* bid for *Rowntree* in 1988.²²³ The public outcry subsequently resulted in a House of Commons debate in which the Secretary of State, *Lord Young*, rejected the idea of reciprocity in no uncertain terms and no reference to the MMC was made: *"To react in that way to this particular bid will not have the slightest effect on Swiss practice. It is an extraordinary way to try to go about changing Swiss practice. For*

220 DTI, Blue Paper on Mergers Policy, para 2.26.

221 *Enserch Corporation and Davy Corporation Ltd*, 1981, Cmnd 8360, para 9.25: *"We foresee detriments to exports and employment arising from the loss of Davy's national character as a British bidder in overseas markets, the lengthening of the chain of management command, and the effects of certain United States legislation."*; *The Hongkong and Shanghai Banking Corporation, Standard Chartered Bank Ltd and The Royal Bank of Scotland Group Ltd*, 1982, Cmnd 8472, para 12.39: *"...transfer of ultimate control of a significant part of the clearing bank system outside the United Kingdom would have the adverse effect of opening up possibilities of divergence of interest which would not otherwise arise."*; *The Government of Kuwait and The British Petroleum Company*, 1988, Cm 477, para 8.117; *Elders IXL Ltd and Allied-Lyons plc*, 1986, Cmnd 9892; *Elders IXL Ltd and Scottish & Newcastle Breweries Plc*, 1989, Cm 654.

For a discussion of some of the cases see Goyder, *Public Interest Criteria*, Fordham 1994, p. 125 134 et seq.

222 DTI, Blue Paper on Mergers Policy, para 2.26.

223 This hostile takeover has obviously turned out to be a success-story, see the retrospection by Lorenz, *Sugar Daddy*, in *Financial Times*, April 20, 1994.

*those reasons, I do not believe that there is any serious point in reciprocity."*²²⁴

However, things were different when issues of greater national importance than chocolate were at stake. In *The Government of Kuwait and British Petroleum Company*, Kuwait's acquisition of a 21.6 per cent stake in *BP* was found to operate against the public interest and Kuwait was required to divest of its holding of *BP* shares to 9.9 per cent: "... while it is not possible to predict the future of the oil markets or the Middle East, we believe that there is a high degree of probability that sooner or later situations will arise in which Kuwait's national and international interests will come sharply into conflict with *BP*'s and the United Kingdom Government's interests. ... We consider that if and when these conflicts occur Kuwait will seek, and be able, to use its shareholding to influence *BP* ... and that this may be expected to be detrimental to, and will operate against, the United Kingdom public interests."²²⁵

In the early 1990s, following a number of bids by mostly French state owned companies for British targets,²²⁶ the issue of foreign state-controlled bidders was the subject of much debate and even led to a formal complaint against the British reference policy on the ground of discrimination to EC Commission by *Crédit Lyonnais*, an aggrieved French state-controlled company.²²⁷ The traditionally liberal approach towards foreign investment was somewhat modified in respect of state-controlled bidders by *Peter Lilley*, then Secretary

224 Hansard, June 8, 1988, column 853.

225 *The Government of Kuwait and The British Petroleum Company*, 1988, Cm 477, para 8.117.

226 French cases: *Crédit Lyonnais SA* and *Woodchester Investments plc*, 1991, Cm 1404; *British Aerospace plc* and *Thomson-CSF SA*, 1991, Cm 1416; *Sligos SA* and *Signet Ltd*, 1991, Cm 1450; *Amoco Corporation* and *Société Nationale Elf Aquitaine*, 1991, Cm 1521. Finnish case: *Kemira Oy* and *Imperial Chemical Industry plc*, 1991, Cm 1406.

227 For a thorough analysis of the issues involved see *Taylor/Bointon/Collison*, U.K. Merger Control and State-controlled Companies, [1991] 4 ECLR 133-138 and *Soames*, Merger Policy: As Clear as Mud?, [1991] 2 ECLR 53, 64-70. Also *Goyder*, Public Interest Criteria, Fordham 1994, p. 125, 132; *Swift/Anderson*, Development in U.K. Competition Law, Fordham 1991, p. 505, 516.

of State.²²⁸ Apparently without previously consulting the MMC he tackled the issue of 'nationalisation through the backdoor' and declared: *"In deciding whether to refer merger situations to the Monopolies and Mergers Commission, I shall in future pay particular close attention to the degree of state-control, if any, of the acquiring party. ... State-controlled companies are not subject to the same disciplines as those in the private sector. They tend to have the assurance of Government backing for their business activities and consequently they do not compete on even terms with private sector companies which operate under the threat of financial failure. Their managements may be motivated to make non-commercial decisions. They may not deploy resources efficiently; and an increase in the resources they manage may well reduce competitive forces. It is important that the MMC should have the chance to consider in detail mergers involving state-controlled companies."*²²⁹ In the wake of the proclamation of the so-called 'Lilley Doctrine' the Secretary of State made five references involving state-controlled bidders to the MMC.²³⁰ Three of these references were made against the advice of the DGFT,²³¹ which is highly unusual.²³² To the embarrassment of the Secretary of State, the MMC subsequently cleared four of the five references - which proved the independence of the MMC. The

228 As to the so-called 'Lilley Doctrine' see *Trade and Industry Committee, First Report, Takeovers and Mergers, 1991*, paras 236-240. The Committee concluded on the issue (para 240): *"We recommend that, before the Secretary of State decides upon any substantial departure from existing reference policy, he should announce his proposals and give interested parties an opportunity to make representations about their merits and practicality."*

229 DTI press notice, July 26, 1990, P/90/457.

230 *Crédit Lyonnais SA and Woodchester Investments plc, 1991, Cm 1404; Kemira Oy and Imperial Chemical Industry plc, 1991, Cm 1406; British Aerospace plc and Thomson-CSF SA, 1991, Cm 1416; Sligos SA and Signet Ltd, 1991, Cm 1450; Amoco Corporation and Société Nationale Elf Aquitaine, 1991, Cm 1521.*

231 *Crédit Lyonnais SA and Woodchester Investments plc, 1991, Cm 1404; Sligos SA and Signet Ltd, 1991, Cm 1450; Société Nationale Elf Aquitaine, 1991, Cm 1521.*

232 See Chapter 6.3.2. at pp. 229 and Table 11 at p. 230.

one merger blocked²³³ was mainly concerned with competition issues and it is arguable that that merger would also have been blocked under pre-Lilley standards.²³⁴

Although Lilley's arguments seem perfectly reasonable, the MMC insisted that under the law as it stands there can be no presumption against a merger, whoever the ultimate owner of a bidder is.²³⁵ Under the Fair Trading Act, each merger has to be considered on its own merits. Where the MMC did not find adverse effects on competition or other public interest issues, the mergers were cleared. Following the formal complaint to the EC Commission against the Lilley Doctrine by *Crédit Lyonnais*, the Secretary of State was forced to declare in a press release by the European Commission: *"When considering whether or not to make a reference to the MMC, the United Kingdom Government examines a range of factors. The fact that a company is state-owned or directed by a state will not per se justify a referral to the MMC; unless exceptionally, other public interest issues (such as security interests) arise, a referral would only be envisaged insofar as competition aspects were at stake."*²³⁶

Albeit the Secretary of State had to climb down on the issue,

233 Kemira Oy and Imperial Chemical Industry plc, 1991, Cm 1406, para 6.85: *"We conclude that the merger would reduce competition in the United Kingdom for agricultural fertilisers. Kemira, already the third largest supplier to the United Kingdom market, would acquire the largest supplier and become market leader. Its market share following the merger cannot be predicted with certainty but could be well over 40 per cent."*

234 Butterworth's Competition Law, Div. VII, para 150.1; Soames, Merger Policy: As Clear as Mud?, [1991] 2 ECLR 53, 66.

235 Crédit Lyonnais SA and Woodchester Investments plc, 1991, Cm 1404, para 8.19: *"Nevertheless, we are unable to accept that we can look at these matters in terms, as has been suggested, of a general presumption. Our approach to the public interest, or to any aspect of it, is governed by section 84(1) of the Act. This provision requires the MMC 'to take into account all matters which appear to them in the particular circumstances to be relevant'. The subsection goes on to require the MMC to have regard to the desirability of five specific matters or objectives. The language of the subsection appears to us to exclude any presumptions, whether of fact or law."*

236 Reproduced in the Appendices to the Minutes of Evidence taken before the Trade and Industry Committee, First Report, 1991, p. 340.

state-control remains a legitimate factor in assessing the public interest. Of course, the EC-Treaty rightly prohibits discrimination on grounds of nationality. But as long as foreign and British state-controlled bidders are treated the same way, i.e. as long as there is no discrimination, the Secretary of State's approach appears sensible. By and large, state-controlled companies are a different breed: the basic capitalistic rule of the survival of the fittest does not apply to them. Clearly, the degree of state control and the individual circumstances matter greatly, but in general state-control appears to be a reasonable ground on which to refer and block a bid.

6.4.3. Countervailing Benefits

As well as affecting the public interest adversely, mergers may also bring about some public interest benefits, for example

- (1) increased efficiency,²³⁷
- (2) increased international competitiveness,²³⁸
- (3) the rescue of a failing firm,²³⁹ and even
- (4) environmental advantages.²⁴⁰

In reaching its conclusion the MMC cautiously takes the beneficial effects into account and weighs them against the adverse effects of a merger, so that public interest detriments can be offset by benefits.²⁴¹ As there is no guidance in section 84 or elsewhere in

237 H Weidmann AG and B S & W Whiteley Ltd, 1975, Cmnd 6208; Prosper De Mulder Ltd and Croda International plc, 1991, Cm 1611.

238 British Airways Plc and British Caledonian Group plc, 1987, Cm 247; Alcatel Cable SA and STC Ltd, 1994, Cm 2477.

239 Swedish Match AB and enterprises belongign to Allegheny International Inc, 1987, Cm 227; Kemira Oy and Imperial Chemical Industry plc, 1991, Cm 1406 (adverse finding). See *Butterworth's Competition Law*, Div. VII, para 169.1.

240 Prosper De Mulder Ltd and Croda International plc, 1991, Cm 1611.

241 See *Finbow/Parr*, U.K. Merger Control, para 6.050 et seq; *Whish/Sufrin*, *Competition Law*, p. 695.

the Fair Trading Act as to the weight to be given to those countervailing benefits, the matter is very much left to the MMC's discretion.

The following excerpt, taken from the report on the acquisition of the animal waste rendering business of Croda at Market Harborough by *Prosper De Mulder (PDM)* may suffice to explain the method applied by the MMC: *"We have concluded that the merger has an adverse effect on competition in the collection of high-grade animal waste in the South-West and South-East of England. ... As for the issues other than competition, the merger is likely to improve PDM's efficiency, and to lead to some wider public health and environmental benefits, as a result of the rationalisation which it enables PDM to achieve in the collection and processing of animal waste. ... Having taken account of the limited adverse effects on competition on the one hand, and the important public issues of health and the environment as well as efficiency gains on the other hand, we conclude that the merger situation which we have identified does not and may be expected not to operate against the public interest."*²⁴²

6.5. Concluding Remarks

The explanations made so far indicate that the tripartite institutional structure has its drawbacks. Of course, fairness and balance of power are by and large guaranteed under the present system, which is why it still has numerous strong supporters. However, work is inevitably duplicated as the merger makes its way through the different merger control stages. The result of this is a protraction of the procedure, the costs of which in terms of expenses and commercial uncertainty come down with the parties to the

242 Prosper De Mulder Ltd and Croda International plc, 1991, Cm 1611, para 6.77, 6.80, and 6.81.

merger. It remains, of course, to be seen in Chapters 7 and 8 whether the unitary system favoured in Germany and Brussel works more effectively.

Another point worth noting is that the part time nature of MMC may not be conducive to the formulation of a consistent merger policy. However, the analysis of the substantive appraisal criteria has shown that despite the broadly defined public interest criterion the focus of the merger control authorities has for the last decade very much been on competition. References based exclusively on other factors are highly exceptional. Of course, public interest issues other than competition may influence the outcome of an investigation in one way or another, but competition is almost always likely to be the decisive factor. Given this emphasis on competition, *John Swift* is right in concluding that U.K. merger policy is more predictable than is generally acknowledged.²⁴³

Clearly, some degree of uncertainty and unpredictability is inherent in the present structure of U.K. merger control both because of the heavy involvement of the Secretary of State, who is after all a politician, and the open-ended and highly flexible public interest criterion applied. However, these uncertainty-factors are somewhat offset by the fact that the Fair Trading Act takes a very liberal approach towards mergers. It has been demonstrated that there is a basic presumption in favour of mergers as private business transactions. The onus of proof clearly rests with the authorities. Hence, only a very small proportion of mergers is finally blocked. As long as British merger policy is that liberal, it seems easy to accept a certain degree of unpredictability. However, if merger policy became under a new government, for example, more interventionist for ideological reasons, the inherent unpredictability would be bitterly felt by industry as there is ample room for political interference in the present structure.

243 *John Swift, Merger Policy: Certainty or Lottery?*, p. 264, 279.

Chapter 7

MERGER CONTROL IN GERMANY

7.1. Introduction

Contrary to Britain where mainly procedural aspects, in particular the institutional framework of merger control, are passionately debated,¹ the institutional structure and procedural aspects of merger control are, broadly speaking, not on the agenda in Germany. An issue constantly gaining more attention, however, is the “europeanization” of German merger control law.² The government is planning a 6th amendment to the German Act against Restraints of Competition (Gesetz gegen Wettbewerbsbeschränkungen, GWB) specifically designed to adjust the German merger control law more to the European Merger Control Regulation.³ This Chapter intends to examine the procedural and substantive German merger control law and to explain the main discrepancies between British and German law.

1 See in particular the *Trade and Industry Committee*, Fifth Report: U.K. Policy on Monopolies, 1995. See also numerous other references in Chapter 6.3. to Chapter 6.3.4. at pp. 220-242.

2 See for example *Dreher*, Das deutsche Kartellrecht vor der Europäisierung, WuW 1995, 881-907; *Möschel*, Reform des europäischen und des deutschen Kartellrechts, EWS 1995, 249, 253 et seq.

3 As to new European developments see Chapter 8.3.2.(4) at pp. 367.

7.1.1. Historical Development

Whereas in England the ancient *restraint of trade doctrine*⁴ prevented to some extent the cartelization and concentration of the economy, German legal history in the 19th and early 20th century is characterized by the absence of such a doctrine.⁵ Rather on the contrary, the *Reichsgericht* decided 1897 in the *Holzstoff-Fabrikanten* case that as part of the fundamental freedom of trade competitors were entitled to enter into cartel agreements.⁶ This legal liberalism and the worldwide economic recession of the 1920s resulted in a growing cartelization and concentration of the German economy to the point of a fully planned and controlled war-economy during the Hitler years.⁷ After the breakdown of the Nazi-dictatorship in 1945 the allied forces demanded the decartelization and deconcentration of the German economy,⁸ which mainly affected the coal and steel industry, the chemical industry, and the film industry. This enforced deconcentration of key-industries was at that time seen by many Germans as a deliberate attempt by the allied forces to weaken the German economy.⁹ Because of these strained political circumstances and despite the fact that the German authorities were already in 1949 asked by the Allies to devise a German anti-trust law, it was not until 1958 that the German Act *against Restraints of Competition* (Gesetz gegen Wettbewerbsbeschränkungen, GWB) came into force. Following a decade of controversial debate the Act prohibited cartels, but did not contain any provisions on substantive merger control in order not to hamper the growth of the economy during the “*Wirtschaftswunder*”

4 *Whish/Sufrin*, Competition Law, p. 48 et seq.

5 *Harms*, in GK, Einleitung Zus.-Kontrolle, Rn. 30, 32; *Paschke*, in FK, vor Sec. 23 Rn. 24.

6 RGZ 38, 155, 158.

7 *Harms*, in GK, Einleitung Zus.-Kontrolle, Rn. 32.

8 U.S. Zone: Gesetz Nr. 56 of 12.2.1947; U.K. Zone: Ordinance No. 78 of 12.2.1947; French Zone: Ordonnance No. 96 of 9.6.1947.

9 *Harms*, in GK, Einleitung Zus.-Kontrolle, Rn. 38.

years.¹⁰ It was considered sufficient to introduce a provision prohibiting the abuse of economic power. The need for additional provisions controlling mergers was not accepted.¹¹ Only notification of certain mergers was required to give the Federal Cartel Office an overview over the degree of concentration in the economy.¹² A coalition government consisting of social democrats and liberals finally introduced substantive merger control provisions in 1973 by way of a second amendment to the GWB.¹³ Although the merger control provisions have since been amended various times,¹⁴ the 1973 framework has remained in place to date. On October 3, 1990 the applicability of the GWB was through the Unification Treaty extended without qualifications to the territory of the former German Democratic Republic.¹⁵ At present, a 6th amendment to the GWB primarily aimed at adjusting the GWB provisions more to the European competition law is being discussed,¹⁶ but thus far no ministerial draft bill has been produced.¹⁷

10 *Mestmäcker*, in Immenga/Mestmäcker, vor § 23 Rn. 4.

11 The Economics Committee as a subcommittee of the House of Parliament (Bundestag) discussed this question in detail at that time: BT-Drucksache (1957) II 1158 and 3644.

12 *Paschke*, in FK, vor § 23 Rn. 30.

13 Second GWB-Amendment of August 3, 1973 (BGBl. I, S. 917) introducing merger control.

14 Third GWB-Amendment of June 28, 1976 (BGBl. I, S. 1697) tightening the control over newspaper mergers. Forth GWB-Amendment of April 4, 1980 (BGBl. I, S. 458) introducing presumptions as to when a dominant position exists. Fifth GWB-Amendment of December 7, 1989 (BGBl. I, S. 2486) extending the definition of what constitutes a merger.

15 Art 8 of the Unification Treaty (BGBl. 1990 II, No. 25, p. 892). For details see Immenga/Mestmäcker, Einleitung Rn. 56 et seq. As to the increase of mergers due to unification see Table 2 at p. 19.

16 See in particular *Dreher*, Das deutsche Kartellrecht vor der Europäisierung, WuW 1995, 881-907; *Möschel*, Reform des europäischen und des deutschen Kartellrechts, EWS 1995, 249, 253 et seq.

17 The Federal Ministry of Economics has, however, published a paper outlining the basic ideas regarding the proposed 6th amendment to the GWB: *Bundesministerium für Wirtschaft*, Eckpunkte für eine Novelle des Gesetzes gegen Wettbewerbsbeschränkungen, May 2, 1996, Geschäftszeichen: I B 5-221200.

7.1.2. Overview over the Merger Control Process

The relevant substantive merger control law is to be found in Part I, Chapter 3 of the GWB under the heading “*Market-Dominating Enterprises*” (see APPENDIX 7). Important procedural provisions are to be found in Part III and Part IV of the GWB. The main merger control statutes, sections 22 to 24b GWB, are lengthy and complex and, due to the frequent amendments, somewhat confusingly arranged. Not surprisingly, high on the agenda for the next amendment of the GWB is the simplification of the current provisions.¹⁸

Excluding the courts, which play contrary to Britain¹⁹ a prominent role in the merger control process in Germany, three different institutions are charged with exercising merger control:

- (1) The Federal Cartel Office
- (2) The Federal Minister of Economics
- (3) The Monopolies Commission

At first glance there seem to be some similarities to the tripartite U.K. institutional framework consisting of the Office of Fair Trading,²⁰ the Monopolies and Mergers Commission,²¹ and the Secretary of State.²² However, this impression is deceptive as the roles played by the German authorities differ widely from those of their British

18 Stellungnahme der Bundesregierung zum *Tätigkeitsbericht des BKartA 1993/1994* vom 15.6.1995, *Bundestag Drucksache* 13/1660.

19 See Chapter 6.4. at pp. 245.

20 See Chapter 6.3.1. at pp. 221.

21 See Chapter 6.3.3. at pp. 229.

22 See Chapter 6.3.2. at pp. 229 and Chapter 6.3.4. at pp. 242.

counterparts.

In principle, any transaction falling under the merger definitions²³ and meeting certain quantitative thresholds, which are turnover-based, is to be notified to the FCO in Berlin.²⁴ If the merger qualifies for investigation,²⁵ it is the FCO's job to establish whether the merger is to be expected to result in or strengthen a dominant market position for the participating enterprises.²⁶ If the merger leads to or strengthens a dominant market position, the FCO *has to* prohibit or, as the case may be, dissolve the merger, unless the participating enterprises demonstrate that the detrimental effects coming with the dominant position are outweighed by improvements in the competitive structure of the markets caused by the merger (balancing-clause).²⁷

In comparison to the British system, a number of points are worthy of note even at this stage. First, the substantive criteria against which mergers are assessed differ: the public interest in Britain²⁸ - market dominance in Germany.²⁹ Secondly, unlike the authorities in Britain,³⁰ the FCO enjoys no discretion in making its decision: if it finds that a dominant position which is not outweighed by competition related advantages has arisen or is being strengthened, it is bound to prohibit or dissolve the merger.³¹ Thirdly, with regard to the balancing-clause it is important to note that contrary to the law in Britain³² only pro-competition effects put forward by the enterprises may be taken into account by the FCO. There is no room for other public interest considerations like regional development and employment, research and development, national

23 See Chapter 7.3.1. at pp. 283.

24 Sec. 23 I and Sec. 24a GWB. See Chapter 7.2.1. at pp. 276.

25 See Chapter 7.3. at pp. 283.

26 Sec. 24 I GWB.

27 Sec. 24 I GWB. See Chapter 7.5.3. at pp. 330.

28 See Chapter 6.4. at pp. 245.

29 See Chapter 7.5.1. at pp. 317.

30 See Chapter 6.3.2. at pp. 229 and Chapter 6.3.4. at pp. 242.

31 Sec. 24 I GWB; *Bechtold*, GWB, § 24 Rn. 38.

32 See Chapter 6.4.3. at pp. 262.

security, foreign state control etc.³³

Appeal against the FCO's decision lies with the Berlin Superior Court, the so-called *Kammergericht*.³⁴ Contrary to the judicial review procedure in Britain,³⁵ the *Kammergericht* is entitled to review the FCO's decision both on a factual and legal basis and is hence empowered to substitute its own decision for that of the FCO.³⁶ A second appeal against the *Kammergericht* decision lies, if leave to appeal is granted, to the Federal Supreme Court (*Bundesgerichtshof*) in Karlsruhe.³⁷ However, this appeal is limited to legal points; factual findings of the FCO and the *Kammergericht* may not be challenged again.³⁸

The parties to a merger may also appeal to the Federal Minister of Economics against the FCO's decision.³⁹ The appeals to the courts and to the Economics Minister are not mutually exclusive, but may not be made at the same time. Hence, the parties may first appeal to the courts and, if unsuccessful, then appeal to the Federal Minister of Economics - and vice versa.⁴⁰ However, as will be explained in further detail in Chapter 7.4.2.,⁴¹ an appeal to the Minister is in most cases hardly worthwhile. Various Economics Ministers have repeatedly made clear that they strictly refuse to be drawn into any conflicts about actual merger cases. Hence, save in

33 See Chapter 7.5.3. at pp. 330. *Kleinmann/Bechtold*, Kommentar zu Fusionskontrolle, § 24 Rn. 100; *Mestmäcker*, in Immenga/Mestmäcker, GWB Kommentar, § 24 Rn. 177.

34 Sec. 62 IV GWB.

35 See Chapter 6.4. at pp. 245.

36 *K. Schmidt*, in Immenga/Mestmäcker, § 62 Rn. 41.

37 Sec. 73 GWB. As to the grounds upon which leave to appeal may be granted see subsection (2) of Sec. 73. Most importantly, leave to appeal may be granted, if a fundamental point of law is raised. Against the decision not to grant leave to appeal, a further appeal is possible, sec. 74 GWB.

38 Sec. 75 II 1. For details see *Karsten Schmidt*, in Immenga/Mestmäcker, GWB Kommentar, § 75 Rn. 5 et seq.

39 Sec. 24 III GWB.

40 *Kleinmann/Bechtold*, Kommentar zu Fusionskontrolle, § 24 Rn. 347; *Mestmäcker*, in Immenga/Mestmäcker, GWB Kommentar, § 24 Rn. 302-304.

41 See pp. 311.

very exceptional cases an appeal to the Federal Minister of Economics can not be considered a passable road for any practical purposes.

The issues which are to be taken into account by the Minister differ completely from those applied by the FCO and the courts.⁴² The issues considered by the Economics Minister resemble, in fact, those public interest issues other than competition applied in Britain. While being legally bound by the FCO's factual and legal findings, in particular in respect to the question of whether the merger is expected to lead to or strengthen a dominant position,⁴³ the Federal Minister of Economics may nevertheless permit the merger if in the individual case the restraint of competition is compensated by *overall economic advantages* of the merger or if the merger is justified by an *overriding public interest*.⁴⁴ Before making his decision the Federal Minister has to refer the case to the Monopolies Commission which is then required to deliver an expert opinion to the Minister to which he has to have regard to.⁴⁵

The appeal-procedure before the Federal Minister of Economics with the advisory role of the Monopolies Commission somewhat resembles the British procedure, and the German provisions were, in fact, influenced by the British model.⁴⁶ However, looked at it more closely the differences in the regulatory frameworks are substantial and any similarities in respect of the Minister's role are superficial as

42 See Chapter 7.4.2. at pp. 311 and Chapter 7.5. at pp. 315.

43 Berlin Superior Court WuW/E OLG 1937, 1938 (Thyssen/Hüller); Economics Minister WuW/E BWM 159, 161 (Thyssen/Hüller); Economics Minister WuW/E BWM 165, 166 (Veba/British Petroleum); Economics Minister WuW/E BWM 185 (VEW/Ruhrkohle); Economics Minister WuW/E BWM 191, 199 (Daimler/MBB). See also *Mestmäcker*, in Immenga/Mestmäcker, § 24 Rn. 318. Critical to the leading opinion *Bechtold*, GWB, § 24 Rn. 50.

44 Sec. 24 III GWB. See Chapter 7.4.2. at pp. 311.

45 Sec. 24b V 7 GWB. See Chapter 7.4.3. at pp. 313.

46 *Mestmäcker*, Funktionen und bisherige Tätigkeit der Monopolkommission; in *Schwerpunkte des Kartellrechts 73/74*, p. 43, 46; *Mestmäcker*, in Immenga/Mestmäcker, § 24b Rn. 1.

will be explained in more detail in Chapter 7.4.2.⁴⁷

To sum up, the FCO plays the dominant role in the German merger control process. Compared to the open-ended public interest criterion used in Britain the FCO has to take a fairly narrow view as it has to focus exclusively on the question of whether the merger is expected to result in or strengthen a dominant market position. If the FCO finds that a dominant market position has arisen or is being strengthened, it has to prohibit or dissolve the merger. There is - at least in theory - no discretion on its part. The underlying purpose of the German regulation is to provide a maximum of predictability in the decision-making process, while the emphasis of the British model appears to be more on flexibility.

7.1.3. Statistics

Turning to statistics, since the introduction of substantive merger control law in Germany in 1973 until the end of 1994 a total of 19.224 mergers were notified to the FCO and subsequently consummated.⁴⁸ During this period the FCO has formally blocked only 108 mergers.⁴⁹ Yet, most of these decisions were challenged in court. In 58 of these cases the FCO decision was upheld in court, i.e. the merger was finally blocked. In 39 cases, however, the FCO decision was quashed or the matter was following the appeal otherwise settled (e.g. withdrawal of the prohibition on part of the FCO). In the remaining six cases ministerial permissions were granted on public interest grounds. For a direct comparison of the number of cases notified in Britain and Germany refer to Table 14 (Notification Statistics) at page 281 (last column). As to the

47 See pp. 311.

48 *Tätigkeitsbericht des BKartA 1993/1994, Bundestag Drucksache 13/1660, p. 148.*

49 *Tätigkeitsbericht des BKartA 1993/1994, Bundestag Drucksache 13/1660, p. 13.*

respective British figures in more detail see Table 10 (OFT Workload) at page 224 and Table 12 (Outcome of References) at page 234.

In 1995 a total of 1.154 mergers were notified to the FCO of which 4 were blocked by the FCO. In eight cases the participating enterprises either withdrew their merger proposal or modified it so as to avoid any conflict with the merger control provisions.⁵⁰

According to a publication of the Ministry of Economic Affairs, between 1973 and 1991 in addition to the formally blocked mergers around 200 mergers were “informally discouraged” by the FCO prior to their consummation.⁵¹ The informal procedure is gaining more and more importance with about 40 mergers “informally discouraged” in 1995 alone.⁵² A parallel development is taking place in Britain where the number of mergers dealt with in the “confidential guidance procedure” has clearly been on the increase during the 1990s.⁵³

The figures mentioned above reveal three interesting points: (1) First, the number of mergers blocked the “hard way” is relatively small.⁵⁴ However, the number of “informally discouraged” merger proposals is quite substantial. Due to the absence of any written, let alone published decisions regarding the informally blocked mergers, these decisions cannot be analysed here. In terms of transparency and accountability of the merger control authorities this development is clearly not to be welcomed. It is also detrimental to the evolution of a coherent merger policy. (2) The second point worthy of note is the heavy involvement of the courts in the merger control process - a feature that differs fundamentally from merger control in Britain. An

50 *Bundesministerium für Wirtschaft*, Eckpunkte für eine Novelle des Gesetzes gegen Wettbewerbsbeschränkungen, May 1996, p. 6.

51 *Bundesministerium für Wirtschaft*, Erfahrungsbericht des Bundeswirtschaftsministeriums über Ministererlaubnis-Verfahren bei Firmen-Fusionen, WuV 1992, 925, 926.

52 Information kindly provided by the FCO in January 1996 (Mr Kiecker).

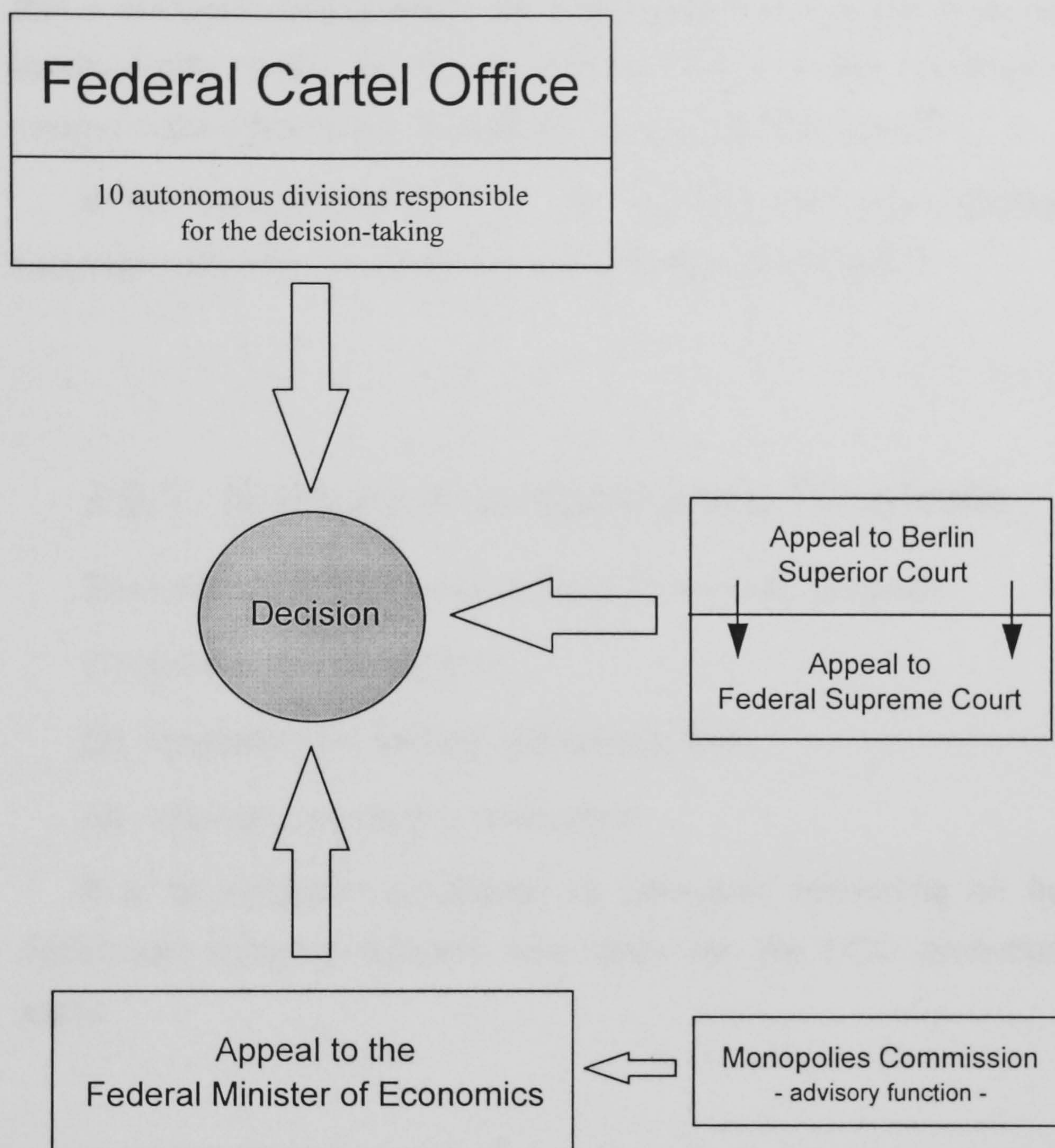
53 See Table 10 at p. 224 and Table 14 at p. 281.

54 As to the situation in Britain see in particular Table 12 at p. 234.

appeal to the courts is very much seen “as part of the game” in Germany. In 1993/1994, for example, the FCO prohibited 7 mergers, all of which were subsequently challenged in court.⁵⁵ (3) Thirdly, the statistics show that the role of the Federal Minister of Economics, who has granted only six permissions on public interest grounds since 1973 with the latest permission being granted as long ago as 1989 is in practice almost negligible.⁵⁶ Needless to say, that the role of the German Economics Minister in the merger control process has therefore very little in common with the part played by his British counterpart.

55 *Tätigkeitsbericht des BKartA 1993/1994, Bundestag Drucksache 13/1660, p. 13.*

56 As to details see Chapter 7.4.2. at pp. 311.



7.2. Notification Requirements

The notification requirement, which has no equivalent in British law,⁵⁷ has been a feature of the German Act against Restraints of Competition since its introduction in 1958, hence long before the implementation of substantive merger control law in 1973.⁵⁸ The

⁵⁷ See Chapter 6.3.1.(1) at pp. 221.

⁵⁸ Harms, in GK, Einleitung Rn. 40; Paschke, in FK, vor § 23 Rn. 30.

notification requirement is therefore to be seen as a set of rules fairly independent of the substantive merger control provisions, meaning that a merger⁵⁹ falling under the notification requirement does not automatically qualify for investigation in terms of the substantive merger control provisions, though this is normally the case.⁶⁰

If the merging parties do not comply with the reporting requirements, they are liable to a fine of up to DM 50.000.⁶¹

7.2.1. Notification Categories and Time-limits

The GWB differentiates in sections 23 and 24a between

- (1) post-merger notification,
- (2) mandatory pre-merger notification, and
- (3) voluntary pre-merger notification.

It is of particular importance to note that depending on the notification category different time limits for the FCO procedure apply.

(1) Post-merger Notification

Systematically and historically, post-merger notification is the principal form of reporting. Nowadays, however, post-merger notification takes place in only about 30 per cent of the cases, the remainder being pre-merger notification cases (see Table 14 at

59 The definition of the term “merger” under German law will be considered in Chapter 7.3.1. at pp. 283.

60 See Table 14 (Notification Statistics) at p. 281.

61 Sec. 39 GWB.

page 281).⁶² Post-merger notification is required where the merging enterprises have had a combined turnover of more than DM 500 million during the last fiscal year.⁶³ Notification has to be filed *without delay* after the merger has been consummated.⁶⁴ The fact that a merger has been consummated is to be published in the Federal Gazette,⁶⁵ although the information provided there is quite limited. Only the names of the merging companies, the type of the merger and the field of business are to be made public.⁶⁶ However, some degree of transparency is ensured that way as the following example taken from the Federal Gazette No. 44/1995 may illustrate:⁶⁷

62 *Tätigkeitsbericht des BKartA 1993/1994, Bundestag Drucksache 13/1660, p. 10.*

63 Sec. 23 I 1 GWB.

64 Sec. 23 I 1 and sec. 39 I 2 GWB.

65 Sec. 10 I No. 4 and sec. 23 V GWB.

66 Sec. 23 V GWB. For details see *Mestmäcker*, in Immenga/Mestmäcker, § 23 Rn. 281-297.

67 This public notice simply states that Deutsche BP Holding, which is a subsidiary of the British Petroleum Company, both of which are operating in the mineral-oil industry, has increased its existing stake in BPM Tankstellenbetriebsgesellschaft, which is running fuel stations, to a majority stake.

Bundeskartellamt

Bekanntmachung Nr. 9/95 über Zusammenschlüsse nach § 23
des Gesetzes gegen Wettbewerbsbeschränkungen
Vom 10. Februar 1995

.....

19.

20. Die von der

The British Petroleum Company plc, London/Großbritannien,

- Mineralölerzeugnisse -

abhängige Deutsche BP Holding AG, Hamburg,

- Mineralölerzeugnisse -

erhöhte ihre Beteiligung auf eine Mehrheitsbeteiligung an der

BPM Tankstellenbetriebsgesellschaft mbH, Dresden,

- Betrieb einer Tankstelle -

21.

From the receipt of the complete notification the FCO than has up to one year to investigate and unravel the merger.⁶⁸ This one-year time limit does not compare too favourably with British law. In Britain the “*period of uncertainty*” is initially limited to only six months as mergers may not be referred to the MMC if they have taken place and made public six or more months before the date of reference.⁶⁹

(2) Mandatory Pre-merger Notification

Mergers have to be notified to the FCO prior to their completion if one of the participating enterprises had turnover proceeds of more than DM 2 billion in the previous fiscal year or if at least two of the

⁶⁸ Sec. 24 II 2 GWB.

⁶⁹ Sec. 64 (4) FTA 1973. See Chapter 6.3.1.(4) at pp. 227.

participating enterprises had each turnover proceeds of more than DM 1 billion during the previous fiscal year.⁷⁰ Hence, pre-merger notification is required only where large deals are concerned. Following the receipt of a complete pre-merger notification the FCO has, in principle, four months within which it may prohibit the merger proposal.⁷¹ Within one month from notification the FCO has to inform the notifying party as to whether it intends to go ahead with the investigation (so-called "first-month-letter"). Otherwise the FCO may not proceed with its investigation. During the four months period the merger may not be consummated unless either permission is granted by the FCO or the "first-month-letter" has not been issued.⁷² Any transactions entered into in contravention of these provisions are void.⁷³ Merger proposals not blocked by the FCO and finally consummated must again be notified to the FCO in accordance with post-merger notification requirements.⁷⁴ In that case a simple letter stating the fact of consummation normally suffices.

The four-months period to investigate large-scale mergers seems acceptable. The participating enterprises may, however, agree to an extension of the four-month period.⁷⁵ In voluntary pre-notification cases in Britain, the Secretary of State must come to a reference decision within twenty days,⁷⁶ but the MMC procedure following has its usual lengths of about three to four months in practice.⁷⁷

70 Sec. 24a I Nos. 1 and 2 GWB.

71 Sec. 24a II 1 GWB. Exceptions to this rule are contained in sec. 24a II 2 Nos. 1-8 GWB.

72 Sec. 24a IV GWB.

73 Sec. 24a IV GWB. *Kleinmann/Bechtold*, Fusionskontrolle, § 24a Rn. 115; *Mestmäcker*, in *Immenga/Mestmäcker*, § 24a Rn. 34.

74 Sec. 24a (3) GWB.

75 Sec. 24a (2) No. 1 GWB. *Ruppelt*, in *Langen/Bunte*, § 24a Rn. 17, 18.

76 Sec. 75B (2) FTA 1973. See *Whish/Sufrin*, Competition Law, p. 686.

77 See Chapter 6.3.3.(4) at pp. 242.

(3) Voluntary Pre-merger Notification

The parties to a merger not reaching the turnover volume requiring mandatory pre-merger notification may choose to notify the FCO voluntarily prior to the consummation of the merger to avoid uncertainties.⁷⁸ In that case, the time-limits discussed in respect of mandatory pre-merger notification cases apply.⁷⁹ However, unlike mandatory pre-merger notification cases, the parties are allowed to consummate the merger during the four-months period. If they do so, the rules and time limits applicable to post-merger notification cases apply.⁸⁰

(4) Notification Statistics

Table 14 and 15 below at page 281 et seq. require little further explanation. The numbers of mergers examined by the German FCO exceed those investigated by the Office of Fair Trading in the U.K. considerably.⁸¹ This is to some extent due to the larger size of Germany the gross domestic product amounting to ECU 1390.80 billion compared to ECU 800.85 billion in Britain in 1994.⁸² Moreover, German unification and the ensuing privatization process in East Germany boosted the number of mergers, which is most visible in 1991 as Table 15 at page 281 indicates. Although allowance has to be made for these factors, it still appears that in respect of notification and preliminary examination of merger cases German merger control law and practice is more stringent.

78 Sec. 24a I 1 GWB.

79 *Mestmäcker*, in Immenga/Mestmäcker, GWB Kommentar, § 24a Rn. 19.

80 *Mestmäcker*, in Immenga/Mestmäcker, GWB Kommentar, § 24a Rn. 19.

81 Table 10 at p. 224.

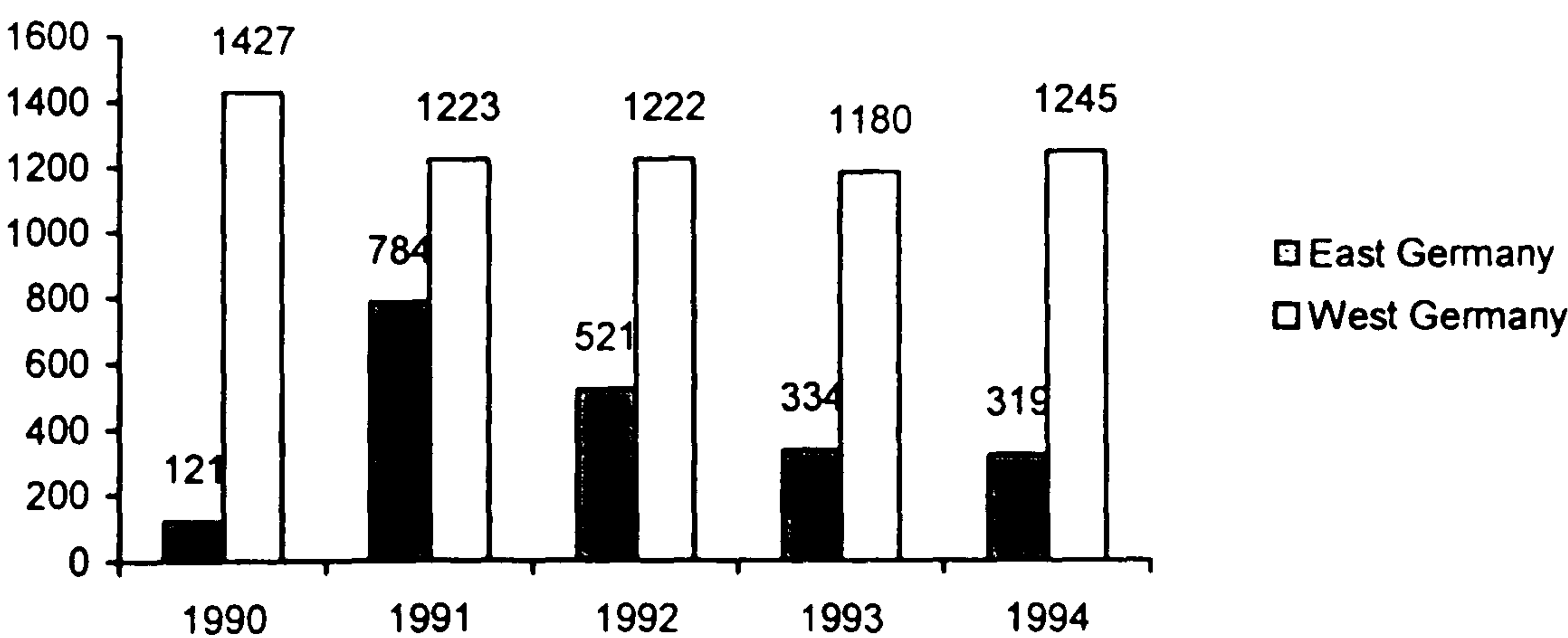
82 *Eurostat*, Eurostatistics, 3/4/5-1996, p. 49.

Table 14: Notification Statistics

Year	Total Number of cases notified and consummated	Cases notified, but <u>not</u> qualifying for investigation	Post-merger notification	Pre-merger notification	OFT: cases examined (qualifying) in the U.K. ⁸³
1986	802	121	184	497	524 (313)
1987	887	183	192	512	478 (321)
1988	1159	247	275	637	456 (306)
1989	1414	269	274	871	427 (281)
1990	1548	221	306	1021	369 (261)
1991	2007	197	351	1459	285 (183)
1992	1743	152	411	1180	200 (125)
1993	1514	154	310	1050	309 (197)
1994	1564	147	331	1086	381 (231)

Source: Tätigkeitsberichte des Bundeskartellamtes and Annual Reports of the DGFT

Table 15: German Unification and Mergers



Source: Tätigkeitsbericht des Bundeskartellamtes 1993/1994

83 For more details refer to Chapter 6.3.1.(1) at pp. 221 and Table 10 at p. 224.

7.2.2. Content of Notification

It is perhaps surprising that no particular filing form exists in Germany. Under European law, the so-called Form CO requires the supply of substantial information.⁸⁴ Even under the relatively lenient merger control regime in Britain, a special form called "*Office of Fair Trading Merger Notice*" requiring rather detailed information exists with respect to voluntary pre-merger notifications.⁸⁵ The information to be filed in Germany, which is identical in post- and pre-merger notification cases, is set out in section 23 (5) GWB (see APPENDIX 7). The amount of data required by the FCO on each of the merging enterprises at this stage is relatively modest. However, the FCO may request further information from the parties, which is normally provided voluntarily.⁸⁶ If not, the FCO has at its disposal very wide ranging and effective investigative powers⁸⁷ which even include the search of the companies' premises provided a search warrant has been granted by the local court.⁸⁸

84 Annex I to the Implementing Regulation 2367/90 of 25 July 1990, [1990] O.J. L219/5, contains Form CO, which specifies the information which must be provided in detail.

85 Available from the OFT, Mergers Secretariat, Field House, 15-25 Breems Buildings, London, England EC4A 1PR. See also S.I. 1990 No. 501: The Merger (Pre-Notification) Regulations 1990. As to non-pre-notification cases see OFT, Mergers: the Content of Submissions, March 1994.

86 Sec. 23 VI GWB.

87 Sec. 46 GWB.

88 For a thorough description of the FCO's powers in English see *Stockmann*, Investigatory Powers of Antitrust Authorities and procedural guarantees under German Law, Fordham 1993, p. 307-336. See also Investigatory Powers, Fact Finding, Procedural Guarantees, Transparency and independence of Antitrust Authorities: Roundtable Two, Fordham 1993, p. 337-372.

7.2.3. Persons Obligated to Notify

In principle, the obligation to notify the FCO lies with the participating enterprises. Who the participating enterprises are for the purpose of notification depends on the type of merger⁸⁹ and is specified in section 23 (4) GWB. In case of an acquisition of shares it is the buyer, the seller, and the target company who are to report.⁹⁰ In practice, it is often internally agreed that the notification for all respective parties is made by only one party, usually the purchaser.

7.3. Mergers Qualifying for Investigation

In order to qualify for investigation three requirements must be fulfilled: First, a transaction must fall under the merger definition (7.3.1.). Secondly, certain quantitative criteria are to be met (7.3.2.). And thirdly, the German authorities have jurisdiction only if there is some territorial link (7.3.3.).

7.3.1. Definition of a Merger

The definition of the term merger is of relevance to both the rules regarding notification and the substantive merger control law.⁹¹

Although British and German law have in common that the term merger is defined in very broad terms, the way the respective provisions are technically drafted differs completely. Under the

89 See Chapter 7.3.1. at pp. 283.

90 Sec. 23 (4) Nr. 2 GWB. *Mestmäcker*, in Immenga/Mestmäcker, § 23 Rn. 279.

91 *Emmerich*, Kartellrecht, p. 357; *Mestmäcker*, in Immenga/Mestmäcker, § 23 Rn. 134.

British Fair Trading Act 1973 a merger is deemed to exist where control of one enterprise - meaning a controlling interest, the ability to control policy or the ability materially to influence policy - passes to another.⁹² Hence, British law uses general broad terms to cover all possible types of transactions without actually attempting to describe them.

German law has traditionally taken a different approach. The GWB undertakes in sections 23 (2) and (3), at least in principle, to describe the different types of business transactions, such as the acquisition of assets, the acquisition of shares or the conclusion of enterprise agreements, constituting mergers exhaustively.⁹³ Any transaction not falling under one of the categories specified in section 23 is not subject to the notification requirement and substantive merger control. The underlying reason for this course has been to provide for a maximum of clarity and predictability, and to ensure a high degree of accountability on the part of the merger control authorities. Although these legal arguments clearly carry some weight, the German approach has at least to some extent failed in practice.⁹⁴ As one would imagine the parties to mergers have often tailored their transactions in such a way as to circumvent the rather inflexible merger definitions of the GWB.⁹⁵ In order to close these loopholes, the government was forced to amend the GWB at various times.⁹⁶ In particular, the Second and Fifth Amendment of the GWB in 1973 and 1990 added two "sweeping-up" provisions which are discussed later.⁹⁷ Hence, the legislative trend is towards the British definition-approach. It is therefore not surprising

92 Sec. 64,65 FTA 1973. See Chapter 6.2.1. at pp. 214.

93 Berlin Superior Court WuW/E 2145, 2146 (Sonntag Aktuell II); *Paschke*, in *Frankfurter Kommentar*, § 23 Rn. 33; *Emmerich*, *Kartellrecht*, p. 357.

94 *Dreher*, *Das deutsche Kartellrecht vor der Europäisierung*, WuW 1995, 881, 904; *Emmerich*, *Kartellrecht*, p. 357, 358.

95 Some notoriety gained the so-called 24.99 per cent-cases. See *Emmerich*, *Kartellrecht*, p. 357.

96 As to the latest amendment see in particular *Paschke*, *Der Zusammenschlußbegriff des Fusionskontrollrechts*, p. 55. Also *Mestmäcker*, in *Immenga/Mestmäcker*, § 23 Rn. 134.

97 See Chapter 7.3.1.(6) at pp. 291.

that the 1990 European Merger Control Regulation did not follow the German example. Under Article 3 (1) of the Regulation a merger is deemed to have occurred where “*direct or indirect control*”, defined as “*decisive influence*”, has been acquired.⁹⁸ The German set of rules defining the term “*Zusammenschluß*” as they stand today reflect the piecemeal development through amendments. They are a somewhat incoherent mixture of precise descriptions of certain types of transactions and more broadly framed clauses designed to close loopholes. It is submitted that the merger definitions in Germany could be simplified substantially. Time appears to be ripe for reform in that respect.⁹⁹ In order to simplify matters and to further European harmonization, the obvious route to take would be to adopt the definition of the European Merger Control Regulation,¹⁰⁰ which will be discussed in more detail in Chapter 8.¹⁰¹

Since the merger definitions play an important role in practice, the following paras provide an overview over the different types of mergers as defined by section 23 (2) and (3) of the GWB.

(1) Acquisition of Assets

The acquisition of assets of another enterprise by way of amalgamations, reconstructions, or by any other means is deemed to constitute a merger if the assets acquired represent the whole or a

98 See Chapter 8.3.1.(2) at pp. 356.

99 *Dreher*, Das deutsche Kartellrecht vor der Europäisierung, WuW 1995, 881, 904; *Emmerich*, Kartellrecht, p. 358.

100 This opinion is to some extent shared by the Ministry of Economics, although it is not intended to simply adopt the European definition. Apparently the ideas circulate around a combination of fixed thresholds and the broad merger definition as used by the European Merger Regulation. See *Bundesministerium für Wirtschaft*, Eckpunkte für eine Novell des GWB, 6 May 1996, Gesch.-Zeichen I B 5 - 221200, pp. 13. In favour of an adoption of the definition of the European Merger Regulation: *Dreher*, Das deutsche Kartellrecht vor der Europäisierung, WuW 1995, 881, 904.

101 See Chapter 8.3.1. at pp. 355.

substantial part of the assets of the selling enterprise, section 23 (2) No. 1 GWB. Clearly, the difficulty with this provision is to determine in an individual case what amounts to a *substantial part* of the assets. Both the Berlin Superior Court (*Kammergericht*) and the Federal Supreme Court in Karlsruhe (*Bundesgerichtshof*) had to deal with this question various times,¹⁰² one of the most remarkable cases probably being the *Kettenstichnähmaschinen* case.¹⁰³ This case concerned the sale of an industrial sewing machine factory. The assets sold accounted for only 0.5 per cent of the total assets of the seller and generated only 1.4 per cent of its total sales. The market share attributable to the assets was about 3.2 per cent. The Federal Supreme Court held - as the Berlin Superior Court had done before - that the key test was not whether the assets acquired represented a substantial part in terms of value in relation to the sellers total assets, but whether the acquired assets would make a tangible difference to the *buyer* with respect to his market position. Hence, the approach taken by the Federal Supreme Court is based more on a qualitative than quantitative assessment. The assets acquired must to some extent represent a functional and organisational unit. The result is a fairly wide interpretation of the term "substantial part", which is very much in line with the British interpretation of the term "enterprise" as used by the Fair Trading Act.¹⁰⁴ In Germany even the acquisition of a mixing plant for bitumen costing only about DM 1.2 million - at that time roughly the price of a large family home as the Berlin Superior Court pointed

102 Berlin Superior Court, WuW/E OLG 1908 and Federal Supreme Court, WuW/E BGH 1570 (*Kettenstichnähmaschinen*); Berlin Superior Court WuW/E OLG 1993 (*Organische Pigmente*); Federal Supreme Court WuW/E BGH 1655 (*Zementmahlanlage II*); Berlin Superior Court WuW/E 2093 and Federal Supreme Court WuW/E BGH 1763 (*Bituminöses Mischgut*); Berlin Superior Court WuW/E OLG 3591 (*Coop Schleswig-Holstein/Deutscher Supermarkt*); Berlin Superior Court WuW/E OLG 2887 (*Krupp/Total*); Berlin Superior Court WuW/E OLG 2007 (*Kunststoffrohre*).

103 Berlin Superior Court, WuW/E OLG 1908 and Federal Supreme Court, WuW/E BGH 1570 (*Kettenstichnähmaschinen*) (1979).

104 See Chapter 6.2.1. at pp. 214. Also sec. 63 (2) and 137 (2) FTA 1973.

out¹⁰⁵ - was held by the Federal Supreme Court to constitute a *substantial part of the assets* in that individual case.¹⁰⁶

(2) Acquisition of Shares

The acquisition of shares as defined by section 23 (2) No. 2 GWB is the most important type of merger transaction in practice (see Table 16 at page 293).¹⁰⁷ Under this provision the acquisition of shares, aggregated with shares already held by the acquiror or affiliated enterprises, meeting or exceeding one of the three following thresholds is deemed to constitute a merger:

- (a) 25 per cent of the capital or voting rights.
- (b) 50 per cent of the capital or voting rights.
- (c) a majority interest within the meaning of section 16 (1) of the Stock Corporation Act 1965, i.e. the majority of the capital or the voting rights.

The way the provision is drafted, (b) is of relevance only where exactly 50 per cent of the voting rights or the capital is acquired. Anything above that limit is falling under (c).¹⁰⁸ As to the calculation of the shareholding, all shares in the target held by enterprises belonging to the corporate group of the acquirer are to be aggregated.¹⁰⁹ The same holds true for those shares held on account of the acquirer by any other enterprise.¹¹⁰ Each passing of one of the aforementioned thresholds triggers the notification requirement anew and, if qualifying for investigation, the substantive

105 Berlin Superior Court WuW/E OLG 2093 (Bituminöses Mischgut).

106 Federal Supreme Court WuW/E BGH 1763 (Bituminöses Mischgut).

107 See also *Emmerich*, Kartellrecht, p. 360. As to the typical nature of shareholdings in Germany see Chapter 2 at pp. 20, Chapter 4.1.2. at pp. 122 and Chapter 4.2.1. at pp. 132.

108 *Bechtold*, GWB, § 23 Rn. 14.

109 Sec. 23 (1) sentence 2 GWB.

110 Sec. 23 (2) No. 2 sentence 2 GWB.

merger control process. In practice stakes just below the relevant threshold figures are often built up. In order to close some of the loopholes, sentence 4 of Section 23 (2) No. 2 stipulates that a merger is deemed to have occurred where the purchaser is afforded by agreement, articles, or resolution a position which is equivalent to that of a minority shareholder holding a blocking minority of at least 25 per cent. Moreover, Nos. 5 and 6 of section 23 (2) are designed to close remaining gaps.¹¹¹

(3) "Joint Ventures"

A particularly far-reaching merger definition which has no equivalent in English or European law is contained in section 23 (2) No. 2 sentence 3 GWB: where two or more companies acquire each - simultaneously or not - stakes exceeding the relevant thresholds (e.g. 25 per cent) in a third company, then a merger is not only deemed to have occurred between each of the acquiring companies and the third company, but separately also between the acquiring companies.¹¹² It is not necessary that the acquiring companies act in concert; they do not even have to know of their respective acquisitions. The underlying reason behind this rule is the so-called "group-effect", i.e. the assumption that the acquiring companies, because of their shared interest in their "joint venture", do not compete as vigorously as before.¹¹³

An example may illustrate this perhaps surprising provision: A-company and B-company acting independently acquire at different

111 See Chapter 7.3.1.(6) at pp. 291.

112 The same applies if a company is set up jointly by two or more companies of each holds at least a 25 per cent stake. See *Emmerich*, Kartellrecht, p. 401.

113 *Bechtold*, GWB, § 23 Rn. 17; *Emmerich*, Kartellrecht, p. 401; *Kleinmann/Bechtold*, Fusionskontrolle, § 23 Rn. 128; *Mestmäcker*, in *Immenga/Mestmäcker*, § 23 Rn. 182.

times each 25 per cent (or more) in C-company. As a result mergers are not only deemed to have occurred between A/C and B/C, but also between A and B.

Details on how to interpret this provision are highly controversial. One dispute revolves around the question whether a more restrictive interpretation is commendable in the context of substantive merger control as opposed to notification.¹¹⁴ Contrary to the FCO,¹¹⁵ the courts have held that in the context of substantive merger control law a merger between the acquiring companies may only be presumed to have occurred where those companies form some sort of *economic unity*.¹¹⁶ Another controversy, which is repeated on European level,¹¹⁷ surrounds the treatment of joint ventures with respect to the general prohibition of cartel agreements as stipulated by section 1 (1) of the GWB.¹¹⁸ One school of thought tries to differentiate between co-operative joint ventures (cartel law) and concentrative joint ventures (merger control)¹¹⁹ which corresponds with the handling of joint ventures under the European Merger Regulation.¹²⁰ As this differentiation is often difficult to make in

114 *Emmerich*, Kartellrecht, p. 368; *Mestmäcker*, in Immenga/Mestmäcker, § 23 Rn. 191.

115 FCO, Tätigkeitsbericht, 1979/1980, p. 25; also Monopolies Commission, 3. Hauptgutachten, Rn. 524 et seq.

116 Federal Supreme Court, WuW/E BGH 1533, 1538 (Erdgas Schwaben); Federal Supreme Court, WuW/E BGH 1763, 1765 (bituminöses Mischgut); Berlin Superior Court, WuW/E OLG 1895, 1899 (Erdgas Schwaben). FCO, AG 1990, 502 (MAN/ENASA).

117 *Scherf*, Konzentrative und kooperative Gemeinschaftsunternehmen im europäischen Kartellrecht, AG 1992, 245-258. Also Chapter 8.3.1.(3) at pp. 360.

118 Sec. 1 (1) GWB: "*Agreements concluded by enterprises or associations of enterprises for a common purpose and resolutions of associations of enterprises are ineffective insofar as they are likely to influence, through restraint of competition, production or market conditions regarding the trade in goods or commercial services.*"

119 FCO, Tätigkeitsbericht 1978, p. 23 et seq.; *Bechtold*, Fusionskontrolle bei Gemeinschaftsunternehmen, BB 1980, 344; *Knöpfle*, Zur Unterscheidung zwischen *Konzentrativen* und kooperativen Gemeinschaftsunternehmen, BB 1980, 654; *Scherf*, *Konzentrative und kooperative Gemeinschaftsunternehmen im europäischen Kartellrecht*, AG 1992, 245, 246.

120 Art. 3 (2) of the Merger Regulation. See also Chapter 8.3. at pp. 354.

practice, the courts¹²¹ and the majority opinion¹²² therefore argue that a joint venture should without qualification be subject to both the law on cartel agreements and merger control law provided it qualifies under both sets of rules. However, there exist ministerial plans to bring German law on joint ventures more in line with the European Merger Regulation.¹²³

(4) Enterprise Agreements

Certain agreements between enterprises specified in section 23 (2) No. 3 GWB are also deemed to constitute mergers. In particular, agreements establishing a contract-based corporate group¹²⁴ within the meaning of the Stock Corporations Act 1965¹²⁵ fall under this provision. Contract based groups have been discussed in more detail in Chapter 4.2.5.¹²⁶ As Table 16 below at page 293 indicates, enterprise agreements do not form a significant part of the mergers investigated by the FCO. They are usually preceded by the acquisition of a qualifying stake in the target company, which falls under section 23 (2) No. 2 GWB. However, if an enterprise agreement following an acquisition of a stake leads to a substantial strengthening of the existing connection between the participating enterprises, the agreement is considered a separate merger subject

121 Federal Supreme Court, WuW/E BGH 2169 (Mischwerke); discussed by *Immenga*, *Gemeinschaftsunternehmen als Kartell und Zusammenschluß*, ZHR 150 (1986), p. 366; also *Karsten Schmidt*, *Gemeinschaftsunternehmen und Recht der Wettbewerbsbeschränkungen*, AG 1987, 333.

122 *Bechtold*, *GWB Kommentar*, § 1 Rn. 23 et seq; *Emmerich*, *Kartellrecht*, p. 369; *Immenga*, in *Immenga/Mestmäcker*, § 1 Rn. 503, 507.

123 See *Bundesministerium für Wirtschaft*, *Eckpunkte für eine Novell des GWB*, 6 May 1996, *Gesch.-Zeichen I B 5 - 221200*, p. 14.

124 For example control contracts, profit transfer contracts, or shop leasing or business transfer contracts. See Chapter 4.2.5. at pp. 151.

125 Sec. 291 and 291 AktG. See APPENDIX 2.

126 See pp. 151.

to notification and merger control again.¹²⁷

(5) Partially Corresponding Managements

Section 23 (2) No. 4 GWB stipulates that, where at least half of the members of a corporate board in two different companies consist of the same persons, the situation is to be regarded as a merger no matter whether the boards concerned are supervisory boards, management boards or any other management organ.¹²⁸ Hence, if half of the directors in a British public company were also members of, say, the supervisory board of a German stock corporation and accounted there for at least half of the supervisory board members, under German law a merger would be deemed to have been created. The practical relevance of this merger type is negligible (see Table 16 at page 293).¹²⁹

(6) Sweeping-up Provisions

If a transaction does not fall under any of the transaction types described above, then - and only then - the FCO may resort to the sweeping-up provision contained in No. 5 of section 23 (2) of the GWB. According to No. 5 any transaction other than the types described in Nos. 1-4 is to be considered a merger if the transaction confers on one enterprise power to exercise directly or indirectly a *dominant influence* over another enterprise.¹³⁰ The dominant

¹²⁷ Sec. 23 (3) sentence 1 GWB.

¹²⁸ As to the two-tier board system in Germany see Chapter 4.2.2. at pp. 133.

¹²⁹ As to theoretical difficulties regarding the interpretation of this provision see *Kleinmann/Bechtold*, Kommentar zur Fusionskontrolle, § 23 Rn. 156; *Paschke*, in FK, § 23 Rn. 70; *Mestmäcker*, in Immenga/Mestmäcker, § 23 Rn. 221.

¹³⁰ As to the meaning of "dominant influence" see sec. 17 AktG (Stock Corporation Act 1965) (APPENDIX 2); Federal Supreme Court, WuW/E

influence must be based on some legal position, for example special rights in the articles or shareholder agreements.¹³¹ A de facto economic influence does not suffice. The “*dominant influence*” required by No. 5 commands a higher degree of control than the power “*materially to influence the policy of a body corporate*” sufficient under section 65 (3) of the British Fair Trading Act.¹³²

However, the ultimate sweeping-up provision, No. 6, stipulates that a transaction, type-wise falling under Nos. 2, 4 or 5, but failing to reach the quantitative criteria required there (e.g. the 25 per cent threshold), may nevertheless constitute a merger if the transaction enables one enterprise to exercise *directly or indirectly an influence which is material with respect to competition*.¹³³ This definition is very broad and in its practical effect rather close to British law.¹³⁴ The dogmatic difference is, however, that under German law the No. 6 definition does apply only in exceptional cases where the preceding definitions contained in Nos. 1 to 5 have failed to cover the transaction in question. Hence, before coming to No. 6 the merger control authorities must consider No. 1 to 5. The British test applying only one standard definition regardless of the specific type of transaction (acquisition of shares, amalgamation, etc.), is clearly more practicable without creating more legal uncertainty than the German rules do. Clearly, the German merger definitions are, because of the piecemeal historical development,¹³⁵ unnecessarily complicated and overdue for reform.¹³⁶

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- 131 BGH 2321, 2323; Berlin Superior Court, WuW/E OLG 1993, 1994 (organische Pigmente).
 131 Bechtold, GWB, § 23 Rn. 27; Emmerich, Kartellrecht, p. 374; Mestmäcker, in Immenga/Mestmäcker, § 23 Rn. 233.
- 132 See Chapter 6.2.1. at pp. 214.
- 133 Because of the relatively low intensity of the corporate union created by the No. 6 types of merger, they are not subject to pre-notification, Sec. 24a I 2 GWB.
- 134 See Chapter 6.2.1. at pp. 214.
- 135 See Chapter 7.3.1. at pp. 283.
- 136 See Bundesministerium für Wirtschaft, Eckpunkte für eine Novell des GWB, 6 May 1996, Gesch.-Zeichen I B 5 - 221200, pp. 13. In favour of an adoption of the definition of the European Merger Regulation: Dreher, Das deutsche Kartellrecht vor der Europäisierung, WuW 1995, 881, 904.

Table 16: Merger Types

Year	Acquisition of Assests	Acquisition of Shares	"Joint Ventures"	Enterprise Agreements	Manage- ment Identity	"Sweeping- up"
1986	172	430	174	11	1	14
1987	211	481	171	17	--	7
1988	260	616	260	13	1	10
1989	323	741	325	17	--	8
1990	280	775	460	17	--	16
1991	501	952	507	34	--	13
1992	320	815	560	21	--	27
1993	290	672	507	23	--	22
1994	295	698	527	15	--	29

Source: Tätigkeitsberichte des Bundeskartellamtes

7.3.2. Quantitative Criteria

As in Britain, mergers are subject to control only if they are of significance in terms of volume. The way, however, the quantitative criteria are defined differs. In Britain either the assets test (worldwide assets taken over exceed £70 million) or the market share test (merging enterprises have at least 25 per cent of the market) must be positively satisfied.¹³⁷ In Germany, however, certain mergers are negatively exempted from control. Unlike Britain, the quantitative criteria applied in Germany relate either to the turnover proceeds of the merging enterprises or the volume of the market concerned.

137 Sec. 64 (1)(b) FTA 1973. See Chapter 6.2.2. at pp. 217.

Hence, these criteria do not directly relate to the volume of the transaction itself, but rather to the size of the companies or markets involved. Albeit the German criteria might be easier to establish as the turnover figures are usually known, in terms of rationale the U.K. criteria seem preferable as they refer directly to the transaction in question which the German criteria do not.

Under section 24 (8) Nos. 1-3 of the GWB the following mergers falling under Nos 1, 2 or 3 are exempted from control:¹³⁸

No. 1: Mergers are exempted from control where the joint turnover proceeds of the participating enterprises amounted to less than DM 500 million in the preceding business year.¹³⁹

No. 2: Mergers are also exempted where an independent company with an annual turnover of not more than DM 50 million merges (voluntarily)¹⁴⁰ with another company. The rationale behind this rule is to allow small and medium sized companies to capitalize on their investment by way of selling the company.¹⁴¹ However, this rather controversial rule resulted in large groups buying rather heavily in small markets which led to a distortion of these markets.¹⁴² Therefore, the Forth Amendment to the GWB (1980) added that this rule shall not apply where the acquiring company has an annual turnover of more than DM 1 billion and the annual turnover of the acquired company amounts to more than DM 4 million.¹⁴³

No. 3: A further exemption is made where so-called "*bagatelle-markets*" are concerned, i.e. markets where the volume of goods or services supplied amount to less than DM 10 million per annum provided the market concerned has been existing for at least five

138 As to the exact wording see APPENDIX 7.

139 As to the calculation of the turnover figures see sec. 23 (1) GWB.

140 This rule does not apply where the acquisition is made in hostile fashion. *Mestmäcker*, in Immenga/*Mestmäcker*, § 24 Rn. 207.

141 *Emmerich*, Kartellrecht, p. 339 and 380.

142 *Emmerich*, Kartellrecht, p. 379.

143 As to the reasons for the restriction see Begründung zum Regierungsentwurf (BT-Dr. 8/2136) und the report of the parliamentary committee (Ausschußbericht BT-Dr. 8/3690).

years (*Bagatellmarktklausel*). The underlying rationale of this rule is that very small markets have little or no significance for the economy as a whole and are therefore not “worthy” of merger control.¹⁴⁴ While there is no similar rule to this effect in Britain, it appears that in practice references concerning very small markets are hardly ever made and the author is not aware of any reference concerning a market worth less than the equivalent of DM 10 million in recent years.¹⁴⁵

7.3.3. Territorial Link

Like Britain, the German merger control authorities may only assume jurisdiction if there is some territorial connection - a principle that follows as a matter of course as otherwise the merger control authorities would not have a legitimate interest in policing the transaction.¹⁴⁶ To establish a territorial link, English law asks whether one of the merging enterprises has been “*carried on in the United Kingdom*”.¹⁴⁷ The approach taken by German law differs: section 98 (2) of the GWB stipulates that the Act shall apply to all restraints of competition which have “*effects*” within Germany even if the restraints were caused by events outside the German territory. This so-called “*effects-doctrine*”¹⁴⁸ focuses on the impact a foreign merger might have on the German market, whereas English law

144 *Mestmäcker*, in Immenga/Mestmäcker, § 24 Rn. 210.

145 In recent years one of the smallest mergers referred concerned the acquisition of Reckitt & Colman by the Sara Lee Corporation (August 1992, Cm 2040). In this case the market for shoe polish products was considered to be worth about £13.5 million (para 1.2 and 6.15). The self-selection sector, in which the merger led to adverse effects, was worth only £5.7 million (para 6.49 Table 2). See also *Finbow/Parr*, U.K. Merger Control, para 4.020.

146 *Rehbinder*, in Immenga/Mestmäcker, § 98 Abs. 2, Rn. 16. As to connecting factors in conflict rules, which section 64 (1) of the English FTA 1973 and section 98 (2) of the German GWB are, see in general see *Stone*, *The Conflict of Laws*, p. 9.

147 Sec. 63 (1) FTA 1973. For details see Chapter 6.2.4. at pp. 254.

148 Auswirkungsprinzip.

concentrates more on the business carried on in Britain by one of the merging enterprises prior to the merger situation. The connecting factors¹⁴⁹ used by English and German law - namely "*business carried on*" versus "*effects*" - are fairly comprehensive. Both concepts appear broad enough to cover any case in which the national merger control authorities could possibly have an interest. The difficulty with section 98 (2) of the GWB has therefore not been that it is too narrow - rather on the contrary. Given the wide scope of section 98 (2) GWB, what really is of importance is the way this provision is interpreted and applied in practice by the relevant authorities. The problem has been - and still is - to find a workable interpretation under which the contours of the jurisdictional reach become clear: with regard to the (extraterritorial) application of national merger control law to international mergers a balance has to be struck between safeguarding legitimate German competition interests which may be affected by foreign mergers on the one hand and the public international law principle of non-intervention in foreign affairs¹⁵⁰ on the other hand.¹⁵¹

149 As to the meaning of this term within the field of conflict of law see *Stone*, *The Conflict of Laws*, p. 9, 385.

150 This principle is protected under Article 25 of the German Constitution as part of the general principles of the law of nations: Berlin Superior Court, WuW/E OLG 3051, 3052 (Morris/Rothmans). *Rehbinder*, in Immenga/Mestmäcker, § 98 (2), Rn. 17.

See also *Brownlie*, *Principles on Public International Law*, p. 291, 292 and Ipsen, *Völkerrecht*, p. 292. With regard to the extraterritorial application of national law the Permanent Court of International Justice held: "... *the first and foremost restriction imposed by international law upon a State is that - failing the existence of a permissive rule to the contrary - it may not exercise its power in any form in the territory of another State. ... It does not, however, follow that international law prohibits a State from exercising jurisdiction in its own territory, in respect of any case which relates to acts which have taken place abroad, and in which it cannot rely on some permissive rule of international law. Such a view would only be tenable if international law contained a general prohibition to States to extend the application of their laws and the jurisdiction of their courts to persons, property and acts outside their territory, and if, as an exception to this general prohibition it allowed States to do so in certain specific cases. ... Far from laying down a general prohibition to the effect that States may not extend the application of their laws and the jurisdiction of their courts to persons, property and acts outside their territory, it leaves them in this respect a wide measure of discretion which is only limited in certain cases by prohibitive rules; as regards other cases, every State*

Unlike Britain, where the jurisdictional question appears not to have caused serious problems in practice, the interpretation of the *effects-doctrine* in German law has been subject to considerable controversy, both among academics and the merger control authorities, but also between the FCO and the courts.¹⁵² One controversy, for example, concerns the question whether and, if so, how tangible the “*effects*” in Germany must be in order to entitle the FCO to prohibit a foreign merger.¹⁵³ This question is of particular relevance in view of the pre-merger notification requirement with its far-reaching consequences¹⁵⁴ and section 23 (3) sentence 4 of the GWB which irrebutably presumes that a merger of two or more parent or holding companies also constitutes a merger between their subsidiaries. With a view to the political implications interference with foreign mergers can have, a restrictive interpretation appears preferable. It is therefore submitted that the “*effects*” on the German market should be tangible and concrete if they are to justify the notification requirement and further actions by the German authorities where two foreign companies merge, i.e. the mere possibility of effects or just potential effects should not be considered sufficient in the context of section 98 (2) GWB.¹⁵⁵ This interpretation seems more or less in line with the approach taken by the British MMC in the *MiTeK Industries Inc/Gang-Nail Systems Inc*¹⁵⁶ case and the policy of the OFT.¹⁵⁷ To avoid misunderstandings: the

remains free to adopt the principles which it regards as best and most suitable.” (PCIJ Ser. A, No. 10 [1927], 18 et seq.

151 *Rehbinder*, in Immenga/Mestmäcker, § 98 (2), Rn. 16 et seq.; Lowe, Extraterritorial Jurisdiction, RabelZ 1988, 157 et seq.

152 See *Heidenhain*, Anmeldung und Untersagung von Auslandszusammenschlüssen, AG 1989, 270 et seq.

153 *Bechtold*, GWB, § 98 Rn. 10; *Rehbinder*, in Immenga/Mestmäcker, § 98 (2), Rn. 63 et seq.

154 See Chapter 7.2.1.(2) at pp. 278.

155 *Bechtold*, GWB, § 98 Rn. 10.

156 *MiTeK Industries Inc and Gang-Nail Systems Inc*, Cm 429, (1988), paras 3.1 and 6.2.

157 In its publication, *Mergers: A guide to the procedures under the FTA 1973*, the OFT states on p. 3: “*at least one of the enterprises must be carried on in the United Kingdom or by or under the control of a body corporate incorporated in the United Kingdom. This means that a merger between two foreign companies may still qualify for investigation where*

prohibition by the FCO of a foreign merger is of a declaratory nature only and does not have any immediate or enforceable consequences within the foreign country.¹⁵⁸

However, the prohibition is a necessary legal pre-condition for any active steps to be taken later by the FCO on German territory against the adverse effects the foreign merger might have in Germany. The four cases discussed below may clarify the law and illustrate the development and problems experienced with the jurisdictional aspect of merger control in Germany.

(1) ***Bayer France/Firestone France***: In the *Bayer/Firestone* case the FCO prohibited a proposed merger between two French companies, namely the proposed acquisition of *Firestone France SA* by *Bayer France SA* without even raising the jurisdictional question.¹⁵⁹ *Bayer France SA* was a subsidiary of the German *Bayer AG* so that there was a territorial link. However, *Firestone's* market share in Germany amounted to only 0.8 and 0.4 per cent of the German synthetic rubber and latex market. Hence, the "effect" on the German market required by section 98 (2) GWB would have been very small indeed. The Berlin Superior Court, therefore, quashed this decision arguing that the case basically was a French merger and that the FCO acted unlawfully by not considering section 98 (2) GWB and the implications of the international public law principle of non-intervention in foreign affairs.¹⁶⁰ Hence, the Berlin Superior Court took a more restrictive and cautious line than

either company controls any enterprise which is carried on or incorporated in the United Kingdom."

158 As to British law see section 90(3) of the FTA 1973 which prevents the Secretary of State from making any orders which would "*have effect so as to apply to any person in relation to his conduct outside the United Kingdom unless that person is a citizen of the United Kingdom....*"

159 FCO, WuW/E BKartA 1837(Bayer France/FireStone France).

160 Berlin Superior Court, WuW/E OLG 2411, 2417 (Bayer France/FireStone France I) and Berlin Superior Court, WuW/E OLG 2419 (Bayer France/FireStone France II).

the FCO.¹⁶¹ As the case took place in 1980, i.e. more than fifteen years ago, there is some probability that the FCO would take a more careful line had it to decide the case again today.

(2) **Philip Morris/Rothmans:** This case involved the acquisition of a 50 per stake by the U.S. company *Philip Morris Inc* in *Rothmans Tobacco Holdings Ltd* of the U.K in 1981. Both *Philip Morris* and *Rothmans* had subsidiaries in Germany, namely the *Philip Morris GmbH* and the *Martin Brinkmann AG* respectively.¹⁶² As the combined market share of the German subsidiaries in the German cigarette market would have risen to 31.2 per cent and led to an oligopoly,¹⁶³ the FCO prohibited the *Philip Morris* (U.S.) - *Rothmans* (U.K.) merger.¹⁶⁴ Having learned from the *Bayer/Firestone* case, the FCO specifically dealt with section 98 (2) and the jurisdictional question, but concluded that the prohibition did not infringe the public international law principle of non-intervention in foreign affairs as the FCO prohibition was declaratory only and would not lead to the *Morris/Rothmans* transaction being automatically void.¹⁶⁵ According to the FCO the prohibition of the foreign merger as a whole was necessary in order to provide for a lawful basis for any actions to be taken against the German subsidiaries of the U.S. - U.K. companies. Again, the Berlin Superior Court took a more restrictive view and repealed the FCO decision partly.¹⁶⁶ It was held that the FCO decision was lawful only in so far as it was directed against the effects the merger would have on German territory. For under section 23 (3) sentence 4 of the GWB the merger of the U.S. - U.K. parent companies was deemed to

161 As to this pattern see: *Emmerich*, Kartellrecht, p. 52.

162 Under section 23 (3) sentence 4 of the GWB the merger of the parent companies deemed to constitute a merger of the subsidiaries.

163 Section 23a (2) No. 2 GWB. The five leading cigarette manufacturers had a market share of 95.4 per cent.

164 FCO, WuW/E BKartA 1943 (Philip Morris/Rothmans).

165 FCO, WuW/E BKartA 1943, 1953 et seq. (Philip Morris/Rothmans).

166 Berlin Superior Court, WuW/E OLG 3051 (Philip Morris/Rothmans).

constitute a merger of their German subsidiaries, only the prohibition of this “*German merger*” was held to be in line with the principle of non-interference in foreign affairs.¹⁶⁷ The case was remitted to the FCO to reconsider this point of law again, but the FCO did not change its view and prohibited in 1985 the merger as a whole arguing that it could only prohibit the transaction as a factual event and that took place between a U.S. and a U.K. company.¹⁶⁸

(3) *Linde/Lansing*: The *Linde/Lansing* case, which took place in 1989, is of interest as it indicates a change in the FCO policy in so far as the FCO now appears to be willing - where practicable - to limit the prohibition of a foreign merger to the effects that merger has within Germany.¹⁶⁹

In *Linde/Lansing*, a case which concerned the market for fork-lift trucks, *Linde Hydraulics Ltd* (U.K.), a subsidiary of the German *Linde AG*, acquired a majority interest in *The Kaye Organisation Ltd* (U.K.) which itself had a German subsidiary, the *Lansing GmbH*. The FCO found that the (English) merger between *Linde Hydraulics Ltd* and *The Kaye Organisation Ltd* would strengthen the already dominant position of *Linde AG* (Germany), mainly, but not only, because *Linde AG* would gain via the British companies *Linde Hydraulics* and *The Kaye Organisation* (indirect) control over *Lansing GmbH*. This time, however, the FCO specifically stated that for reasons of public international law it saw itself not in a position to prohibit the (English) merger as a whole, albeit this would have been necessary to prevent any strengthening of *Linde AG*’s dominant position.¹⁷⁰ However, in order to block at least the most damaging

167 Berlin Superior Court, WuW/E OLG 3051, 3053 et seq. (Philip Morris/Rothmans).

168 See FCO, WuW/E BKartA 2204, 2210 (Philip Morris/Rothmans II).

169 FCO, WuW/E BKartA 2363 et seq. (*Linde/Lansing*). See also *Heidenhain*, Anmeldung und Untersagung von Auslandszusammenschlüssen, AG 1989, 270.

170 FCO, WuW/E BKartA 2363, 2369 (*Linde/Lansing*).

effects on competition in the German market, the FCO decided that *Lansing GmbH* must not remain part of the *Linde* group. Although this decision did not hinder any strengthening of *Linde AG*'s dominant decision, it was an agreeable compromise which struck a balance between pure competition aspects on the one hand and the sensitive issue of non-intervention in foreign affairs on the other hand. However, a decision as solomonic as in *Linde/Lansing* is not possible in every case as the next example shows.

(4) *Gillette/Wilkinson*: This case involved a complex international transaction at the heart of which laid *Gillette*'s attempt to win control over *Wilkinson*'s world-wide wet-shaving business in 1990. As *Gillette* and *Wilkinson Sword* are the main global players in the wet-shaving market, the events led not only to an investigation by the U.S. anti-trust authorities, but also to a report by the British MMC¹⁷¹ and a decision by the German FCO¹⁷² which provides the opportunity to make some direct comparisons.

Put simply, *Gillette U.K. Ltd* acquired a 22.9 per cent stake in the Dutch company *Eemland Holdings N.V.*¹⁷³ which was the parent company of the *Wilkinson Sword* group, including, inter alia, *Wilkinson Sword Inc* (U.S.A.), *Wilkinson Sword Ltd* (U.K.), and *Wilkinson Sword Europe GmbH* (Germany). Although the 22.9 per cent stake consisted of non-voting shares only, *Gillette* reserved for itself a number of important continuing rights and interests in *Eemland Holdings N.V.*, including pre-emption and conversion rights, which in effect enabled it to materially influence *Eemland*'s and,

171 MMC, *Stora Kopparbergs Bergslags AB /Swedish Match N.V. and Stora Kopparbergs Bergslags AB/The Gillette Company*, Cm 1473 (1991), para 7.23.

172 FCO, AG 1992, 363 et seq. (*Gillette/Wilkinson*).

173 *Eemland* later (in April 1990) changed its name to *Swedish Match N.V.* which is why the MMC - unlike the FCO - uses this name. See MMC, *Stora Kopparbergs Bergslags AB /Swedish Match N.V. and Stora Kopparbergs Bergslags AB/The Gillette Company*, Cm 1473 (1991), para 7.23.

thus, *Wilkinson's* policy.¹⁷⁴

From the U.K. point of view the jurisdictional question was not an issue in this case as the acquiring party was incorporated in the U.K. This was slightly more difficult for the German merger control authorities as no German company was directly involved. However, as *Gillette* and *Wilkinson* were the main competitors in the German wet-shaving market - together having a market share of well over 90 per cent - and *Eemland* being the owner of *Wilkinson Sword Europe GmbH* in Germany, the merger would have had a considerable "effect" within the meaning of section 98 (2) GWB on competition in the German market.

As the merger would have had an adverse effect on competition in both the British and the German market, the relevant merger control authorities of both countries found against it. Unlike the previous case, however, the FCO prohibited the Anglo/Dutch merger as a whole arguing that it was not possible to confine the prohibition to the effect the merger would have in Germany. In particular a disposal by *Eemland* of the German *Wilkinson Sword Europe GmbH* was not practicable for this company was according to the FCO economically not viable independently of the international *Wilkinson* group. The question of the public international law principle of non-interference in foreign affairs was not raised. As the British blocked the merger anyway the case was probably not as sensitive as, for example, the French *Bayer/Firestone* case discussed above where the French cleared "their" merger, while the German FCO (originally) blocked it.

In substance, the MMC report and the FCO decision very much came to the same conclusions with regard to the evaluation of the transaction and its effect on competition in the respective markets.

174 As to details concerning the *Gillette/Eemland* agreements see in English: MMC, *Stora Kopparbergs Bergslags AB /Swedish Match N.V. and Stora Kopparbergs Bergslags AB/The Gillette Company*, Cm 1473 (1991), para 7.53. In German: FCO, AG 1992, 363, 365 (*Gillette/Wilkinson*).

Formally, however, they differ. As usual, the MMC report contains more than 100 pages (excluding appendices) while the FCO decision is - as usual - rather short, hardly exceeding half a dozen pages. What differs too is the date of publication: the MMC report was published in March 1991¹⁷⁵ whereas the FCO decision - concerning exactly the same events - was taken in July 1992. Making these direct comparisons is, however, not entirely fair as the functions of the MMC and the FCO differ. The FCO's function - which will be explained in more detail later¹⁷⁶ - is to deliver an administrative decision to the participating parties.¹⁷⁷ The MMC's duty is to carry out an in-depth investigation and to deliver a report giving a full and exact picture of the events to the Secretary of State, the parties involved, and the wider public.¹⁷⁸

To sum up, the application of the GWB to foreign mergers which have effects within Germany has been and will continue to be a difficult and sensitive issue. Ultimately, the problems arise from an asymmetrical development which is not only confined to Germany: markets and companies become increasingly international while the merger control authorities stay (largely) national. Of course, the international public law principle of non-intervention in foreign affairs should be strictly adhered to. But adherence to this principle may in certain cases lead to a dilemma as the national merger control authorities may not be able to do anything against manifest adverse effects a foreign merger may have in the home market. In order to circumvent the application of the anti-trust laws of a particular jurisdiction, large multinational enterprises may deliberately tailor their transactions accordingly and exploit this weakness inherent in

175 As to the MMC timing see Chapter 6.3.3.(4) at pp. 242.

176 See Chapter 7.4.1. at pp. 304.

177 Section 24 (2) GWB.

178 See Chapter 6.3.3.(1) at pp. 234.

the concept of different national merger control jurisdiction.¹⁷⁹ Yet, as long as there are no effective supra-national merger control authorities able to control multi-national transactions effectively, this probably is the price to pay for the luxury of keeping an (almost purely) national merger control system. As to the developments on European level which partly mitigate this situation see Chapter 8.¹⁸⁰

7.4. Procedural Aspects

As has been pointed out earlier, the merger control procedure in Germany is dominated by the FCO, which will be reflected in the following representations. The Monopolies Commission comes into play only in those highly exceptional cases where an appeal to the Federal Minister of Economics is made.

7.4.1. The Federal Cartel Office

The FCO, established under the GWB and located in Berlin,¹⁸¹ is the competent authority to police mergers and other restraints of competition on federal level.¹⁸² The FCO's duty with regard to merger control is to examine whether a merger creates or strengthens, or may be expected to create or strengthen, a dominant market position. If it reaches an adverse conclusion, it has to prohibit

179 As to this aspect in Connection with the European Merger Control Regulation see Chapter 8.2.1. at pp. 344.

180 See pp. 335.

181 Sec. 48 GWB. Address: Bundeskartellamt, Mehringdamm 129, 10965 Berlin, Telefon 0049/30/695800, Fax 0049/30/69580400.

182 In particular cartels which exceed the territory of a single Federal State. Cartels affecting only one Federal State are policed by the State Cartel Office (Landeskartellbehörde). As far as merger control is concerned, however, the competence rests exclusively with the FCO in Berlin, sec. 44 (1) No. 1 GWB.

the merger and, as the case may be, to remedy the adverse effects of a consummated merger.

The following paras will discuss (1) the status of the FCO, (2) its personnel and resources, and finally (3) its internal organisation. The substantive criteria applied by the FCO in assessing a merger will be discussed at a later stage (Chapter 7.5.1.).¹⁸³

(1) Status of the FCO

The FCO is a so-called Superior Federal Authority (*Bundesoberbehörde*).¹⁸⁴ It belongs to the portfolio of the Federal Minister of Economics, but its status as a Superior Federal Authority guarantees a high measure of independence from ministerial or political interference. Although the Federal Minister of Economics may give General Instructions (*Allgemeine Weisungen*), which have to be published in the Federal Gazette,¹⁸⁵ he may not interfere in actual merger cases or withdraw competences from the FCO.¹⁸⁶ In practice, political interference in merger decisions of the FCO has because of the status of the FCO apparently never been a problem.

¹⁸³ See pp. 317.

¹⁸⁴ Sec. 48 (1) GWB and Article 87 (3) of the German Consitution (*Grundgesetz*).

¹⁸⁵ Sec. 49 GWB. To date the Federal Minister has issued only five general instructions of which only two are still of relevance to date: (1) General Instruction of 30.3.1976 on undertakings in the merger control procedure, Federal Gazette (BA*nz.*) No. 66 of 3.4.1976 and (2) General Instruction of 30.5.1980 on the handling of foreign mergers, Federal Gazette (BA*nz.*) No. 103 of 7.6.1980. This latter General Instruction requires the FCO to inform the merging parties as soon as possible if it becomes clear for whatever reasons that a proposed merger is not going to be blocked. In the case of foreign participants the FCO has to do so even if the merging parties have failed to provide all the information required under the pre-notification provisions if the notifying foreign party demonstrates at the time of notification that, due to foreign legal provisions or other reasons, it has been prevented from supplying all the required particulars. However, this General Instruction does not free foreign parties from making a full report pursuant to sec. 23 (5) GWB upon consummation of the merger.

¹⁸⁶ See *Klaue*, in Immenga/Mestmäcker, § 48, Rn. 14.

(2) Personnel and Resources

The status of the FCO as an independent Superior Federal Authority engenders that the FCO has its own budget. In 1992 the total expenses amounted to DM 20.06 million (while the revenue from fines and fees added up to DM 21.25 million).¹⁸⁷ About one third of these resources, i.e. around DM 6.6 million, were spent on merger control. A direct comparison with the expenses of the British merger control authorities is difficult as mergers are policed by three different authorities in Britain. By and large, the FCO combines the functions of the OFT, the MMC and the Secretary of State. The OFT spent in 1994 about £0.8 million on merger control¹⁸⁸ and the expenditure of the MMC in the financial year 1994/1995 amounted to £6.8 million.¹⁸⁹

The FCO employs about 252 permanent staff. Roughly 110 thereof, of which half are lawyers and economists, are senior staff (*Beamte und Angestellte des höheren Dienstes*). Around 75 members of staff are exclusively charged with merger control.¹⁹⁰ In addition there are about 13 Members of permanent staff employed by the German Monopolies Commission. In comparison, in the financial year 1994 the average number of permanent staff employed by the OFT was 420, hence, about 170 more than the FCO! However, the number of staff belonging to the so-called Mergers Secretariat of the OFT was relatively small with less than 20 staff.¹⁹¹ A further 77 full-time and 9 part-time staff were employed by

187 Source: Publication of the FCO: "Das Bundeskartellamt", Pressestelle. Publication obtained in January 1996.

188 See Chapter 6.3.1.(2) at pp. 224.

189 See Chapter 6.3.3.(2) at pp. 235.

190 Information provided by the FCO in January 1996 (Mr Foth).

191 Annual Report of the DGFT 1994, p. 92.

the MMC.¹⁹² Although it appears safe to say that the competition authorities in Britain employ more staff than their counterparts in Germany, with respect to merger control the differences seem rather modest. Britain employs roughly 100 (less than 20 OFT plus 77 and 9 part-time MMC) while Germany has only a few less (75 FCO, 13 Monopolies Commission).

(3) Internal Organisation of the FCO

Page 310 shows the organisation chart of the FCO as published in the biennial Report 1994/1995 of the FCO.¹⁹³ Headed by a president and a vice-president and further subdivided into a number of "*Referate*" (sections) dealing with general policy matters the FCO-divisions most important in the present context are the so-called "*Beschlußabteilungen*" (decision-units) of which there are ten each responsible for a different sector of industry. These decision-units, and not the President or Vice-President of the FCO, are under the provisions of the GWB exclusively in charge of the FCO decision-making.¹⁹⁴ The procedure before the decision-units is quasi-judicial, and there is no room for lobbying.¹⁹⁵ The decision-units decide in bodies composed of a Chairman and two Associates. The Chairman should as a general rule be qualified to exercise the functions of a judge, i.e. he must have passed the first and the second legal state examination (*Assessor iur.*). The associates must either be qualified to exercise the functions of a judge or qualified for a position in the senior civil service (non-legal state exam). Furthermore, to ensure their independence, the Chairmen and the Associates of the

192 Annual Report of the DGFT 1994, p. 93. See also Chapter 6.3.3.(2) at pp. 235.

193 Sec. 50 GWB. So-called Tätigkeitsberichte des Bundeskartellamtes.

194 Sec. 48 (3) GWB.

195 *Haidenhein*, in *Investigatory Powers, Fact Finding etc*, Fordham 1993, p. 337, 340. As to the role of lobbying in Britain see Chapter 3.4.3. at p. 91.

decision-units have to be civil servants appointed for life.¹⁹⁶ To avoid any conflict of interest, the GWB specifically provides that the members of the FCO must not be owners, managers or members of the board of management or the supervisory board of an enterprise, a cartel or a business or professional association.

Hence, not only the FCO as a Federal Superior Authority enjoys a relatively high degree of independence from ministerial interference, the internal organisation of the FCO also undertakes to guarantee that those actually responsible for making the decisions are independent from inside and outside pressure and not entangled in any conflict of interest.

The organisational structure as outlined above contrasts sharply with the British approach in two ways. (1) First, as to the investigative stage of the merger assessment, the MMC relies on part-time Members appointed on a part-time secondment basis from senior posts in the private sector.¹⁹⁷ This ensures that top people with different backgrounds can be attracted to make contributions to the merger control process. On the other hand the risk of conflict of interest is inherent in the British system and the so appointed Members may often not be experts on merger control.¹⁹⁸ The way merger control is organised in Britain and Germany is, however, not just a procedural matter, but a reflection of a more deeply rooted difference in the legal culture. As has already been demonstrated with respect to the regulation of takeover bids, as a regulatory principle Britain tends to rely more heavily on the idea of self-regulation and co-operation between regulator and industry stressing the need for a flexible regulatory approach, while in Germany predictability and independence appear to be the overriding legal values. The way the MMC is organized, with “private” part-time

196 Sec. 48 (4) GWB.

197 See Chapter 6.3.3.(2) at pp. 235. As to the background of the MMC Members see Table 13 at p. 239.

198 See Chapter 6.3.3.(2) at pp. 235 and the criticism of the *Trade and Industry Committee* reported there.

Members making through the MMC-Reports weighty recommendations to the Secretary of State, clearly contains a self-regulatory element, although, of course, the MMC being based on the Fair Trading Act 1973 is not a self-regulatory authority in the strict sense of the word. The opposite holds true for the FCO as there is no self-regulatory element whatsoever. In fact, the GWB insisting on life-time civil servants declares personal involvement of FCO members with industry illegal. (2) The second fundamental difference has already been pointed out in Chapter 6.5.¹⁹⁹ and refers to the political aspect of merger control. In Britain, merger control is under the current legal framework ultimately structured as a political matter. This is not only reflected in the open-ended “public interest” criterion applied by the merger control authorities, but mainly by the fact that both the reference decision²⁰⁰ and the final blocking decision²⁰¹ are ultimately made by the Secretary of State for Trade and Industry. In Germany, however, merger control is principally seen as an administrative matter with the FCO enjoying a large measure of independence. However, as has been mentioned earlier,²⁰² the Federal Minister of Economics also has a (minor) role to play in the German merger control process, which will be briefly examined in the following paras.

199 See pp. 263.

200 Chapter 6.3.2. at pp. 229.

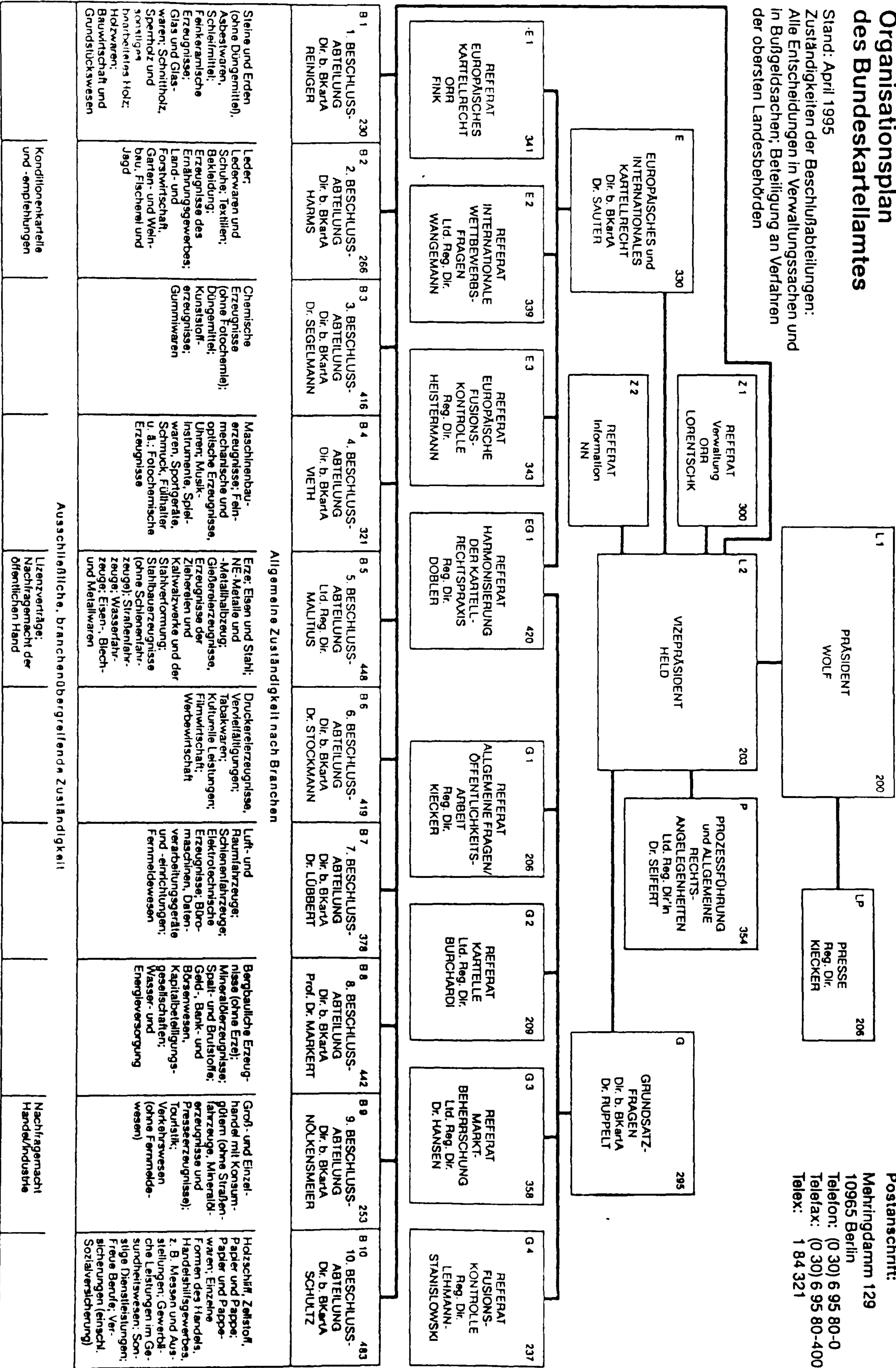
201 Chapter 6.3.4. at pp. 242.

202 Chapter 7.1.2. at pp. 268.

Organisationsplan
des Bundeskartellamtes

Stand: April 1995
Zuständigkeiten der Beschlußabteilungen:
Alle Entscheidungen in Verwaltungssachen und
in Bußgeldsachen; Beteiligung an Verfahren
der obersten Landesbehörden

Postanschrift:
Mehringdamm 129
10965 Berlin
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7.4.2. The Federal Minister of Economics

The role of the Federal Minister of Economics as outlined above²⁰³ differs in two major respects from that of the British Secretary of State.

(1) The first dissimilarity concerns the substantive appraisal criteria to be applied by the Minister. Unlike his British colleague with respect to the MMC-Reports, the German Minister of Economics is bound by the legal and factual findings of the FCO and the courts as to the existence of a dominant market position.²⁰⁴ Contrary to the Secretary of State, the Minister may not overrule the findings of the FCO and the courts.²⁰⁵ He may only permit a merger on grounds other than those taken into account by the FCO and the courts. Section 24 (3) of the GWB defines the appraisal criteria to be applied by the Minister as follows:

“The Federal Minister of Economics shall, on application, grant permission for the merger, if in the individual case the restraint of competition is compensated by the overall economic advantages of the merger or if the merger is justified by an overriding public interest; in this context, regard shall also be given to the competitive capability of the participating enterprises in markets outside the territory in which this Act applies. The permission may only be granted if the scope of the restraint of competition does not endanger the principle of the market economy.”

Since the FCO and the courts are by law prevented from taking these issues into account as they are regarded as of a political nature, there can be no overlap between the aspects the FCO and

203 Chapter 7.1.2. at pp. 268.

204 *Erfahrungsbericht des Bundeswirtschaftsministeriums*, WuW 1992, 925-932. *Bechtold*, GWB Kommentar, § 24, Rn. 50; *Emmerich*, Kartellrecht, p. 425; *Mestmäcker*, in Immenga/Mestmäcker, § 24 Rn. 318.

205 As to U.K. law see Chapter 6.3.2. at pp. 229 and Chapter 6.3.4. at pp. 242.

the courts on the one hand and the Minister on the other hand take into consideration (*dominant market position versus overall economic advantages and overriding public interest*). Consequently, conflicting decisions in the strict sense of the word are not possible as the grounds on which the decisions are taken differ by definition. In Britain, conflicting decisions by the DGFT, the MMC, and the Secretary of State may occur, though this does not happen frequently, as their decisions are based on the same legal grounds, namely the *public interest* as defined in section 84 of the Fair Trading Act.²⁰⁶

(2) Unlike the Secretary of State, the German Minister of Economics gets involved only if, following a prohibition by the FCO, an appeal is made to him. As has been mentioned,²⁰⁷ since the introduction of merger control in 1973 only 15 appeals, of which only 2 have been fully and 4 partly successful, have been launched (see Table 17 at page 315).²⁰⁸ The latest ministerial permission granted concerned the highly controversial merger in the defence industry between mighty *Daimler Benz* and *Messerschmitt/Bölkow/Blohm* (MBB) in 1989.²⁰⁹ Before that, the latest permission granted dates back to 1981 when *IBH-Holding*, a construction equipment group, merged with *Wibau* (and went bust shortly afterwards).²¹⁰ All other permissions concerned cases in the 1970s as Table 17 at page 315 shows. In 1993, 1994, and 1995 not a single appeal has been made to the Minister. The reason for the very limited practical relevance of the ministerial appeal procedure is of a political nature. Any

206 Chapter 6.3.2. at pp. 229.

207 Chapter 7.1.3. at pp. 272.

208 *Tätigkeitsbericht des BKartA 1993/1994, Bundestag Drucksache 13/1660*, p. 13.

209 FCO prohibition: Beschluß des BKartA vom 17.4.1989, WuW/E BKartA 2335. Ministerial permission: Verfügung des Bundesministers für Wirtschaft vom 6.9.1989, WuW/E BWB 191 (Daimler/MBB).

210 FCO prohibition: Beschluß des BKartA vom 3.7.1981, WuW/E BKartA 1892. Ministerial permission: Verfügung des Bundesministers für Wirtschaft vom 9.12.1981, WuW/E BWB 177 (IBH/Wibau).

involvement of the Minister in a merger case is regarded with great suspicion by the wider public and likely to damage the Minister politically.²¹¹ Given this political climate in Germany and the fact that the Minister's past experiences with permissions granted were rather discouraging,²¹² Ministers have repeatedly made very clear their unwillingness to be drawn into disputes over actual merger cases.

7.4.3. The Monopolies Commission

The Monopolies Commission,²¹³ which was vaguely modelled after the British MMC,²¹⁴ becomes involved in the merger control process only if an appeal is made to Federal Minister of Economics.²¹⁵ Unlike the British MMC, which can by not coming to an adverse conclusion in its report prevent the Secretary of State from blocking a merger,²¹⁶ the German Monopolies Commission has a purely advisory function. The Minister is not bound by the recommendation given to him as Table 17 at page 315 shows. Since the ministerial appeal procedure is of very limited practical relevance these days, so is the complementary advisory role of the Monopolies Commission in the merger control process. A few words on the Monopolies Commission may therefore suffice.²¹⁷

211 As to harsh criticism concerning the permission of the Daimler-Benz/MBB merger see, for example, the Parliamentary motion by members of the SPD opposition party: *Deutscher Bundestag*, Drucksache 11/4518. Answer by the Government: *Deutscher Bundestag*, Drucksache 11/5232. See also *Der Spiegel*, 36/1989, p. 116 and 37/1989, p. 110-116.

212 *Erfahrungsbericht des Bundeswirtschaftsministeriums*, WuW 1992, 925, 927. *Emmerich*, Kartellrecht, p. 423.

213 Address: Monopolkommission, Generalsekretär Dr. Horst Greiffenberg, Barbarastraße 1, 50735 Köln, Telefon 0049/221/7581148, Fax: 0049/221/758/2811.

214 *Mestmäcker*, Funktionen und bisherige Tätigkeit der Monopolkommission, Schwerpunkte des Kartellrechts 1974/75, pp. 43, 46.

215 Chapter 7.1.2. at pp. 268.

216 Chapter 6.3.3.(1) at pp. 234.

217 For a more detailed analysis in German see *Kantzenbach*, Zehn Jahre Monopolkommission, WuW 1984, 5-15; *Mestmäcker*, , Funktionen und

The Monopolies Commission consists of five Members appointed for a four year term of office by the Federal President upon designation by the Federal Government.²¹⁸ The Members “*must have particular knowledge and experience in the fields of economics, business administration, social policy, technology or business law.*”²¹⁹ The five Members are supported by seven permanent research staff headed by a Director General and about five administrative staff. The Members of the Monopolies Commission may neither belong to the Government nor the legislature of either the federation or a state, or any other legal entity under public law.²²⁰ Nor may they belong to an employee or employers organization. In making its report the Monopolies Commission is bound only by the mandate established under the GWB.²²¹ Hence, the law places great emphasis on the independence of the Monopolies Commission. The merger reports of the Commission differ in size ranging from less than 50²²² to more than a 150 pages.²²³

bisherige Tätigkeit der Monopolkommission, Schwerpunkte des Kartellrechts 1974/75, p. 43-56.

218 Sec. 24b (6) GWB.

219 Sec. 24b (1) GWB.

220 Sec. 24b (2) GWB.

221 Sec. 24b (4) GWB.

222 E.g. Zusammenschlußvorhaben MAN/Sulzer, Sondergutachten 19, 1990.

223 For example: Zusammenschlußvorhaben Daimler/MBB, Sondergutachten 18, 1989.

Table 17: Ministerial Permissions 1973-1995

Nos.	Case	Applica- tion Date	Monopolies Commission Report	Ministerial Permission
1	Veba/Gelsenberg	9.1.74	not recommended	granted
2	VAW/Kaiser/ Preussag	24.1.75	not recommended	not granted
3	Babcock/Artos	28.4.76	not recommended	granted with modifications
4	Thyssen/Hüller- Hille	27.1.77	recommended with modifications	granted with modifications
5	Sachs/GKN	21.3.78	—	application withdrawn
6	VEBA/BP	4.10.78	not recommended	granted with modifications
7	IBH/Wibau	7.8.81	recommended	granted
8	Burda/Springer	17.11.81	not recommended	application withdrawn
9	Klöckner/SEN	8.11.84	not recommended	application withdrawn
10	VEW/Sidechar	19.7.85	not recommended	not granted
11	Rheinmetall/ WMF	23.7.85	—	application withdrawn
12	Daimler/MBB	2.5.89	recommended with modifications	granted with modifications
13	MAN/Sulzer	20.9.89	not recommended	not granted
14	Daimler/MAN/ Enasa	14.8.90	—	application withdrawn
15	Baywa/WLZ	29.1.92	not recommended	not granted

Source: Erfahrungsbericht des Bundeswirtschaftsministeriums, WuW 1992, 932

7.5. The Substantive Appraisal Criteria

Unlike the British Fair Trading Act under which merger control is based on the broad public interest concept which allows the MMC “to take into account all matters which appear to them in the particular

circumstances to be relevant",²²⁴ the German GWB takes in section 24 (1) - roughly in line with the EC Merger Control Regulation²²⁵ - a comparatively narrow view focusing on the question of whether the merger leads, or may be expected to lead, to *market domination* by the participating enterprises.²²⁶

However, it is not only the rather manifest difference in the underlying substantive concepts - *public interest* versus *market domination* - which differs. At a deeper rooted level it is the incongruous perceptions of the nature of merger control which have a fundamental effect on the substantive merger evaluation. Contrary to Britain where merger control is structured as a highly discretionary affair ultimately of a political nature as only the Secretary of State may refer and block a merger, merger control in Germany is seen distinctly as an administrative matter resting with the FCO and the courts.²²⁷ As a result, German merger control law is drafted as to ensure a maximum of predictability - to some extent necessarily at the expense of flexibility. For that reason the FCO, finding that a merger would lead to or strengthen a dominant market position, has to prohibit the merger legally with no room for discretion.²²⁸ In that respect German law is strict. Another element stemming from the administrative nature of merger control and designed to ensure greater predictability with no equivalent in British law or under the European Merger Control Regulation is the existence of legal presumptions as to when a market dominating position has arisen.

The following paras will mainly focus on the concept of market domination and the criteria applied assessing it (7.5.1.). The function

224 Sec. 84 (1) FTA 1973.

225 Art 2 (3) EC Merger Regulation. See Chapter 8.4. at pp. 377.

226 Sec. 24 (1), 22 GWB.

227 As to the neglectable role of the Federal Minister of Economics and the Monopolies Commission see Chapter 7.4.2 at pp. 311 and Chapter 7.4.3. at pp. 313.

228 Berlin Superior Court, WuW/E 3137, 3140 (Rheinmetall-WMF); *Emmerich*, Kartellrecht, p. 383; Rittner, Wettbewerbs- und Kartellrecht, § 13 para 130.

of the legal presumptions contained in the GWB (7.5.2.) and the so-called balancing clause (7.5.3.) will be discussed in a more cursory way as their importance is rather limited in practice. It will not be specifically dealt with the special provisions on oligopolies.²²⁹

7.5.1. Creation or Strengthening of a Market-Dominating Position

Section 24 (1) of the GWB stipulates that a merger which either creates or strengthens a market dominating position is to be prohibited by the FCO unless the participating enterprises demonstrate that through the merger competition improvements in the respective market which outweigh the detriments arise.²³⁰ Unlike Britain, public interest factors other than those related to market domination may not be taken into account by the FCO. Those other public interest factors, if they exist, are supposed not to have any bearing on the merger assessment by the FCO and, as the case may be, the courts.

(1) Definition of Market Domination

Section 22 (1) No. 1 and No. 2 of the GWB define what is meant

229 See sec. 22 (2), 22 (3) No. 3, 23a (2) GWB. See also FCO, Checklist, Part II. For a leading case on oligopolies see Federal Supreme Court, WuW/E BGH 2433 (Gruner+Jahr/Zeit II).

230 Section 24 (1) GWB: *"If it is to be expected that a merger will result in or strengthen a market dominating position, the Cartel Authority shall have the powers set forth in the following provisions, unless the participating enterprises demonstrate that, by means of the merger, improvements of the competitive conditions will also occur and that these improvements will outweigh the disadvantages of market domination."*

by the term *market-dominating position*.²³¹ The first alternative, No. 1, provides that a market-dominating position is deemed to exist where an enterprise has no competitors in the relevant market or where no substantial competition exists. This subsection as interpreted by the FCO and the courts covers extreme and obvious cases of market power only and has therefore been of relatively limited relevance in practice.²³²

Of much greater practical relevance is the independent second alternative, No. 2, which states that an enterprise is to be considered market-dominating if it “*has a paramount market position in relation to its competitors.*” Methodically similar to section 84 of the British Fair Trading Act,²³³ a number of non-exhaustive²³⁴ exemplary criteria are specified. No. 2 postulates that in determining whether an enterprise enjoys a paramount market position

“in addition to its market share, regard shall be given in particular to its financial strength, its access to the supply and sales markets, its inter-relationships with other enterprises as well as to legal or factual barriers to the entry of other enterprises into the market, the ability to

231 Section 22 GWB is not directly concerned with merger control, but designed only to restrict the abuse of power by market-dominating enterprises. Under German law monopolization through internal growth is not illegal and, unlike Britain, monopolies can not be dissolved. Only abusive practices may be prohibited. As the concept of market domination is defined in section 22, section 24 (1) GWB, the principal substantive merger control provision, makes use of that by simply referring to section 22. As the law uses the same definition of market domination for both the control of abusive practices by dominant enterprises and merger control the difficult question arises whether, in fact, the concept of market domination really is identical in both contexts. It is generally accepted that in determining market dominance in the context of merger control the emphasis is much more on the structural market factors (market share, financial strength etc.) than on the actual behaviour of the competitors (market conduct). For details see *Mestmäcker*, in Immenga/Mestmäcker, § 24 Rn. 25 et seq.; *Ruppelt*, in Langen/Bunte, § 24 Rn. 12.

232 FCO, WuW/E BKartA 1716, 1717 (Kartoffelstärke: 70 % market share); Federal Supreme Court, WuW/E BGH 1685, 1692 (Springer-Elbe Wochenblatt: 80 % market share); FCO, WuW/E BKartA 1561, 1564 (o.b.: 80 % market share); FCO, WuW/E BKartA 2405, 2408 (MAN-Sulzer: 90 % market share). As to the relation between No. 1 and No. 2 of sec. 22 (1) GWB see *Möschel*, in Immenga/Mestmäcker, § 22 Rn. 52.

233 See Chapter 6.4. at pp. 245.

234 Federal Supreme Court, WuW/E BGH 1435, 1439 (Vitamin-B 12). Also v. *Gamm*, § 22 Rn. 27; *Ruppelt*, in Langen/Bunte, § 22 Rn. 46.

*shift its supply or demand to other goods or commercial services, as well as the possibility of the opposite market side to change to other enterprises."*²³⁵

The criteria used to define a paramount market position are distinct structural criteria based on the structure of the market in question. They do not include actual market-behaviour or the intensity of actual or potential competition as this is left to No. 1. Consequently, even the existence of substantial competition does not rule out a paramount market-position.²³⁶ In this respect, the emphasis of substantive German merger control law differs from British law where the degree of competition in the respective market is *the* key-factor in assessing whether a merger operates, or may be expected to operate, against the public interest.²³⁷ Broadly speaking, the approach taken by the British merger control authorities is much more in line with No. 1 of section 22 (1) GWB (no substantial competition) than with No. 2 of section 22 (1) GWB. The bottom-line question in assessing mergers in Germany is, whether the enterprise "*due to market- or firm-related structural criteria has a scope of action which is not sufficiently controlled by its competitors.*"²³⁸

Taking section 22 (1) No. 2 as a starting point, over the years a considerable body of case law consisting of FCO and court decisions has developed which makes it possible to classify those factors of major importance and, notwithstanding deviations in individual cases, to indentify a certain order of priority. Taking account of the decisions of the FCO and the courts as well as the legal and economic thinking on the issue, the FCO has in 1990 produced a

235 These criteria were introduced by the Second Amendment to the GWB in 1973 (BGBl. 1973 I S. 917) and last modified by the Fifth Amendment to the GWB in 1989 (BGBl. I S. 2486). See *Möschel*, in Immenga/Mestmäcker, § 22 Rn. 59.

236 Federal Supreme Court, WuW/E BGH 1445, 1449 (Valium); FCO, Checklist, I. (Introductory Remarks); *Möschel*, in Immenga/Mestmäcker, § 22 Rn. 59.

237 See Chapter 6.4.1.

238 FCO, Checklist, I. (Introductory Remarks).

fairly extensive brochure called “*Checklist for Merger Control Procedures*” in order to provide guidance to the business community. The *Checklist* is because of its practical importance reproduced in its English version in APPENDIX 8.²³⁹ Regarding single-firm market domination the *Checklist* singles out nine factors:

- (1) *Market share*
- (2) *Financial strength*
- (3) *Access to supply or sales markets*
- (4) *Interlocks*
- (5) *Barriers to market entry*
- (6) *Competition from imperfect substitutes*
- (7) *Foreign competitors*
- (8) *Buying power on the opposite side of the market*
- (9) *Market phase*

As not all of these factors can be discussed in detail here, the following representations concentrate on the criteria *market share* and *financial strength* as these factors are undisputedly of pre-eminent weight in the evaluation of mergers in Germany.²⁴⁰ All other factors are, broadly speaking, confined to a complementary role.²⁴¹ As a rule, these other factors may only *strengthen* an already existing market-dominating position, but do not create it in the first place. In practice, a finding of market domination will not be based exclusively on factors other than market share and financial strength. However, in assessing market domination an overall appraisal of the competitive market conditions taking account of both detrimental and beneficial effects of the merger is required.²⁴² In this context it

239 This brochure is available in English and can be obtained from the FCO.

240 *Ruppelt*, in *Langen/Bunte*, § 22 Rn. 48; *Möschel*, in *Immenga/Mestmäcker*, § 22 Rn. 63.

241 FCO, Checklist I.10: “*If a firm’s market share and financial strength are insufficient evidence of its paramount scope of action, the remaining conditions of competition may still give the firm a decisive advantage over its competitors.*” Berlin Superior Court, WuW/E OLG 2889 (Krupp-Total).

242 Federal Supreme Court, WuW/E BGH 1445, 1449 (Valium); Federal Supreme Court, WuW/E BGH 1435, 1439 (Vitamin-B 12); Federal

depends quite like in Britain very much on the individual case which factors are to be given decisive weight. A paramount scope of action as indicated by a significant market share may, for example, be offset by a rival's financial strength.

(a) Market Share

The market share based on the turnover-percentage²⁴³ achieved by the enterprise in the relevant market has always been the single most important indicator in assessing market domination.²⁴⁴ This is partly due to the economic fact that there usually is a correlation between market share and economic power.²⁴⁵ The particular importance of the market share criterion in Germany, however, stems from the provisions of the GWB. First, the market share criterion ranks first among the exemplary criteria specified in No. 2 of section 22 (1) GWB. Secondly, and even more importantly, an enterprise is according to section 22 (3) No. 1 GWB *presumed* to be market-dominating if its market share reaches one-third of the market (unless its turnover proceeds were below DM 250 million in the last preceding year). The exact meaning of this presumption has been the subject of some debate.²⁴⁶ It is undisputed, however, that the 1/3 threshold is not to be seen as an irrebuttable presumption automatically leading to a finding of market

Supreme Court, WuW/E BGH 1749, 1755 f (Klöckner-Becorit). For further details see FCO, Checklist I.10 (APPENDIX 8).

243 The calculation of the market share is based on turnover figures and not on the quantity of the products sold: Berlin Superior Court, WuW/E OLG 2053, 2057 (Valium) and Federal Supreme Court, WuW/E BGH 1678, 1681 (Valium II).

244 *Möschel*, in Immenga/Mestmäcker, § 22 Rn. 59.

245 Federal Supreme Court, WuW/E BGH 1501, 1503 (Kfz-Kupplungen); Federal Supreme Court, WuW/E BGH 1749, 1755 (Klöckner-Becorit); Federal Supreme Court, WuW/E BGH 2575, 2580 (Kampffmeyer-Plange); Berlin Superior Court, WuW/E OLG 2182, 2185 (hydraulischer Schreitausbau).

246 For a detailed discussion see *Möschel*, in Immenga/Mestmäcker, § 22 Rn. 91, 92.

domination. Nor does the burden of proof as to market domination, which rests with the FCO, shift to the merging enterprises once the 1/3 level is exceeded. According to the leading opinion section 22 (3) is of relevance directly only where an FCO or court investigation leads to a *non-liquet* concerning market domination²⁴⁷ which not often is the case in practice.²⁴⁸ However, the 1/3 threshold can be seen as a rule-of-thumb-indication of when the law considers an enterprise to be market-dominating. In practice, the FCO and the courts deal with the market share criterion in a fairly flexible way, although the weight attributed to the market share criterion in Germany very clearly exceeds that in Britain where the parameter market share is treated with more reserve.²⁴⁹

In any case an *overall appraisal of the competitive conditions* is required by the FCO and the courts.²⁵⁰ It is therefore rarely the market share criterion alone which determines the outcome of a merger investigation. Thus, neither guarantees a low market share the clearance of a merger nor does a market share above the 1/3 threshold necessarily lead to an adverse finding. In the *Rewe-Florimex* case concerning the import and wholesale market for cut flowers, for example, the FCO²⁵¹ and the Berlin Superior Court²⁵² both found that despite a relatively low market share of only about

247 Federal Supreme, Court WuW/E BGH 1501, 1503 (Kfz-Kupplungen); Federal Supreme, Court WuW/E BGH 1749, 1755 (Klöckner-Becorit); Federal Supreme, Court WuW/E BGH 2231, 2237 (Kaufhof/Saturn); Berlin Superior Court, WuW/E OLG 1745, 1751 (Sachs); Berlin Superior Court, WuW/E OLG 2234, 2235 (Blei- und Silberhütte Braubach); FCO, WuW/E BKartA 1799, 1800 (Blei- und Silberhütte Braubach); FCO, WuW/E BKartA 2414, 2417 (WMF-Hutschenreuther); FCO, WuW/E BKartA 2421, 2425 (Unilever-Braun); *Kleinmann/Bechtold*, § 22 Rn. 223 et seq.; *Möschel*, in Immenga/Mestmäcker, § 22 Rn. 92; *Ruppelt*, in Langen/Bunte, § 22 Rn. 62.

248 See, however, FCO, WuW/E BKartA 1457, 1461 (Veba-Gelsenberg).

249 Chapter 6.4.1.(1) at pp. 247. *OFT, Mergers: A guide to the procedures under the FTA 1973*, p. 10-11; *OFT, Mergers: The Content of Submissions*, para 12. *Finbow/Parr*, U.K. Merger Control, p. 202 et seq.

250 Federal Supreme Court, WuW/E BGH 1445, 1449 (Valium); Federal Supreme Court, WuW/E BGH 1435, 1439 (Vitamin-B 12); Federal Supreme Court, WuW/E BGH 1749, 1755 f (Klöckner-Becorit); FCO, Checklist I.10 (APPENDIX 8).

251 FCO WuW/E BKartA 1876 (Rewe-Florimex).

252 Berlin Superior Court, WuW/E OLG 2862, 2864 (Rewe-Florimex).

12 per cent *Florimex* were to be considered market-dominating as it was provided with considerable financial resources and had easy access to international supply-markets while the remaining competitors in the market were much smaller most of them securing market shares of only around 0.25 per cent. Conversely, in *Revell Plastics* a market share of between 35-40 per cent was held not to be enough to create a market-dominating position because in that case a number of strong competitors, one having a market share of around 22 to 25 per cent, were active on the market and barriers to entry for new competitors were relatively low.²⁵³ Hence, like in Britain it depends very much on the circumstances of the individual case whether a particular level of market share gives rise to an adverse finding, although the probability of an enterprise exceeding the 1/3 market-share threshold not being considered market dominating is comparatively low.²⁵⁴ In assessing whether a merger leads to or strengthens a *dominant market position* the market share is the key-criterion in Germany, while in Britain, where the *public interest* is the touchstone of merger control, the market share criterion is not reaching the weight it has in Germany.

(b) Financial Strength

The second most important criterion in assessing market domination is the financial strength of the enterprises concerned.²⁵⁵

253 Federal Supreme Court, WuW/E BGH 1620, 1621 (*Revell Plastics*). (not a merger case).

254 See also FCO, WuW/E BKartA 1657 (*Rheinstahl-Hüller*: 34 per cent = market domination); FCO WuW/E BKartA 1727, 1729 (*RWE-Energieversorgung Leverkusen*: 25 per cent = market domination); FCO WuW/E BKartA 1695 (*Uran*: 25 per cent = no market domination); Berlin Superior Court WuW/E OLG 2887, 2890 (*Krupp-Total*: 31,4 per cent = no market domination).

255 Federal Supreme Court, WuW/E BGH 1749, 1755 f (*Klöckner-Becorit*); Federal Supreme Court, WuW/E BGH 1501, 1503 (*Kfz-Kupplungen*); Federal Supreme Court, WuW/E BGH 2150, 2156 (*Edelstahlbestecke*); Federal Supreme Court, WuW/E BGH 2575, 2580 (*Kampffmeyer-*

The relevance of this criterion is not confined to conglomerate and vertical mergers, but also plays a role in assessing horizontal mergers.²⁵⁶ The financial strength criterion has no direct equivalent in the assessment of mergers in the U.K. although under the rubric *remaining competitors* their financial resources are considered.²⁵⁷

The financial strength criterion is named in section 22 (1) No. 2 GWB, but there is no legal or otherwise exact definition of the term. In practice, a number of factors are taken into account in order to assess the financial strength of an enterprise,²⁵⁸ most notably its turnover²⁵⁹ and cash-flow (net earnings, plus depreciation and other allowances).²⁶⁰ The method applied in assessing the financial strength is from an economist's point of view²⁶¹ therefore probably somewhat unsystematical which is not surprising given that merger control is at least at court-level, and to some extent also in the FCO,²⁶² in the hands of lawyers rather than economists.

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- Plange); Berlin Superior Court, WuW/E OLG 1937, 1938 (Thyssen/Hüller); FCO WuW/E BKartA 1711, 1717 (Mannesmann-Brueninghaus)
- 256 *Emmerich*, Kartellrecht, p. 396.
- 257 See Chapter 6.4.1.(2) and *MMC*, Assessing Competition, para 13.
- 258 The Official Government Reasons for the 2nd Amendment to the GWB, Begründung zum Regierungsentwurf der 2. GWB-Novelle, BT-Drucksache VI/2520, S. 23, state that in assessing the financial strength of an enterprise "*the whole of the financial means and possibilities of an enterprise, in particular its financing possibilities (equity and debt financing) and its access the capital markets*" are to be taken into account.
The FCO-Checklist states: "*A firm's financial strength is determined by its possibilities of equity and debt financing. It may be assessed by measures such as turnover, profit, cash flow, net operating margin, credit line, access to national or international capital markets, and other criteria.*", para I.2. See also *Möschel*, in Immenga/Mestmäcker, § 22 Rn. 64; *Ruppelt*, in Langen/Bunte, § 22 Rn. 49.
- 259 Federal Supreme Court, WuW/E BGH 2150, 2157 (Edelstahlbestecke); Berlin Superior Court, WuW/E OLG 3137, 3146 (Rheinmetall-WMF).
- 260 FCO, WuW/E BKartA 1625, 1628 (GKN-Sachs); FCO, WuW/E BKartA 1727, 1729 (RWE-Energieversorgung); FCO, WuW/E BKartA 1711, 1717 (Mannesmann-Brueninghaus). *Möschel*, in Immenga/Mestmäcker, § 22 Rn. 64; *Ruppelt*, in Langen/Bunte, § 22 Rn. 49; *Bühner*, Die fusionskontrollrechtliche Bedeutung der Finanzkraft, WuW 1989, 277, 281.
- 261 *Treis/Eggers*, Überragende Marktstellung aufgrund von Finanzmacht, GRUR 1988, 745.
- 262 See Chapter 7.4.1.(2) and (3) at pp. 306.

The relative weight attributed to the financial strength criterion is theoretically justified by the prevailing opinion with the so-called *deterrence-doctrine*,²⁶³ basically meaning that potential entrants might be deterred from entering the market while actual smaller competitors might be discouraged from further active competition against a giant-company. This is based on the assumption that a very large enterprise is provided with superior staying power, the power to compete more aggressively (predatory pricing), and to spend more on research and advertising. Hence, the *deterrence-doctrine* is in essence based on a prognosis as to the psychological effects the existence of a financially dominating competitor might have within the market.²⁶⁴ Consequently, the soundness of this doctrine is extremely difficult to verify in practice.²⁶⁵ There has also been plausible criticism both from an economic and legal point of view concerning the *deterrence-doctrine*. Economically, the assumption has been challenged that superior financial power of a competitor is necessarily detrimental to competition in a particular market. On the contrary, it has been argued that increased financial power usually leads to increased rentability which in turn spurs competition.²⁶⁶ Legally, the point has been made, that the constitutional rights of property and freedom of economic action guarantee that a decision as economically important and far reaching for the merging enterprises as the blocking of a merger should not be based on a rather speculative and empirically unverified²⁶⁷ element

263 Harms, in GK, § 24 Rn. 457 et seq.; Kleinmann/Bechtold, Fusionskontrolle, § 22 Rn. 175 et seq.; Möschel, in Immenga/Mestmäcker, § 22 Rn. 63; Ruppelt, in Langen/Bunte, § 22 Rn. 49

264 Emmerich, Kartellrecht, p. 396; Knöpfle, Wird die Marktbeherrschende Stellung eines Unternehmens durch dessen Aufnahme in einen finanzstarken Konzern verstärkt?, BB Beilage 5/1985, p. 1, 3 et seq.

265 See for an empirical study, however, Bühner, Die fusionskontrollrechtliche Bedeutung der Finanzkraft, WuW 1989, 277, 284. Bühner concludes that diversification and superior financial strength have very little impact on the competitive situation in the respective market.

266 Treis/Eggers, Übertagende Marktstellung aufgrund von Finanzkraft, GRUR 1989, 745, 748.

267 Bühner, Die fusionskontrollrechtliche Bedeutung der Finanzkraft, WuW 1989, 277, 284.

like the discouraging psychological effects flowing from a financially powerful competitor.²⁶⁸ Hence, it appears arguable that the criterion *financial strength* is overrated in Germany.

(2) Creation or Strengthening

A merger is to be prohibited if a market-dominating position is either created or strengthened, section 24 (1) GWB. A paramount market position is created if the merger leads to a market position as described above which would not exist otherwise. It is strengthened if the merger “*further deteriorates the conditions of competition on the market concerned*.”²⁶⁹ This is most notably the case if the merger increases the market share of an already market dominating enterprise. If an enterprise has a market dominating position, horizontal mergers by such enterprises are highly likely to be prohibited “*almost on a per se basis*.”²⁷⁰ Yet, even without any increase in market share, the FCO and the courts may come to the conclusion that a market-dominating position is strengthened if its scope for autonomous action in the market is widened which may be the case in particular where the financial resources of an already market-dominating enterprise are boosted so as to discourage actual or potential competitors (deterrence-doctrine).²⁷¹ Regarding the

268 *Knöpfe*, Wird die Marktbeherrschende Stellung eines Unternehmens durch dessen Aufnahme in einen finanzstarken Konzern verstärkt?, BB Beilage 5/1985, p. 1, 3 et seq.

269 FCO, Checklist, I. (Introductory Remarks).

270 *Markert*, Merger Control in Germany: Substantive Aspects, Fordham, 1990, p. 149, 157.

271 Federal Supreme Court, WuW/E BGH 2150, 2157 (Edelstahlbestecke); Federal Supreme Court, WuW/E BGH 1501, 1503 (Kfz-Kupplungen); Federal Supreme Court, WuW/E BGH 1655, 1659 (Zementmahlanlage II). See also: FCO, WuW/E BKartA 2363, 2367 (Linde/Lansing): a strengthening of the market position abroad through an international merger may also be considered a strengthening of market-dominating position on the national market. *Emmerich*, Kartellrecht, p. 393. As to the deterrence-doctrine see Chapter 7.5.1.(1)(b).

degree of strengthening necessary, German law is strict as a *tangible* or *substantial* deterioration of the conditions of competition is not required by the FCO and the courts.²⁷² A market share increase of between 1 and 4 per cent may suffice.²⁷³

7.5.2. Legal Presumptions

Unlike the British Fair Trading Act the German GWB contains a number of legal presumptions.²⁷⁴ Section 22 (3) No. 1 GWB according to which it is to be presumed that an enterprise having a market share exceeding 1/3 is in a market-dominating position has already been discussed.²⁷⁵ In 1980 following proposals of the Monopolies Commission²⁷⁶ the Fourth Amendment to the GWB introduced section 23a (1) containing three more monopoly presumptions which were mainly aimed at vertical and conglomerate mergers, but do also apply to horizontal concentrations.²⁷⁷ Contrary to section 22 (3) where it is only presumed that a market-dominating position exists, section 23a (1) presumes that a paramount market position as defined by section 22 (1) No. 2 is being *created* or *strengthened*.

The presumptions contained in Section 23a (1) will be discussed

272 Federal Supreme Court, WuW/E BGH 1501, 1512 (Kfz-Kupplungen); Federal Supreme Court, WuW/E BGH 1655, 1659 (Zementmahlanlage II); Berlin Superior Court, WuW/E OLG 3137, 3146 (Rheinmetall-WMF); Federal Supreme Court, WuW/E BGH 1685, 1691 (Springer-Elbe Wochenblatt). Critical: *Harms*, in GK, § 24 Rn. 334.

273 Federal Supreme Court, WuW/E BGH 1685, 1691 (Springer-Elbe Wochenblatt: 1,3 % market share increase); Federal Supreme Court, WuW/E BGH 1655, 1659 (Zementmahlanlage II: 4 % increase). *Emmerich*, Kartellrecht, p. 397.

274 The following paras are confined to monopoly-presumptions. It will not be dealt with the oligopoly-presumptions contained in sec. 22 (3) No. 2 and sec. 23a (2) GWB.

275 Chapter 7.5.1.(1)(b) at pp. 323.

276 *Monopolkommission*, Hauptgutachten I, 1976, Rn. 952, 957, 960 and Hauptgutachten II, 1978, Rn. 466.

277 *Bechtold*, § 23a, Rn. 1; *Ruppelt*, in *Langen/Bunte*, § 23a Rn. 2.

in a rather cursory way as their practical relevance has been limited,²⁷⁸ the FCO and the courts clearly being reluctant to base decisions as grave as the blocking of a merger on a presumption rather than an overall appraisal of the relevant factors. As with section 22 (3) the presumptions are directly applicable only in *non-liquet-cases*, i.e. in cases where the FCO or court investigation has not come to any definite conclusions regarding the creation or strengthening of a market-dominating position.²⁷⁹ Furthermore, the presumptions can, of course, be rebutted by the merging enterprises if they demonstrate that the factors generally used to substantiate a paramount market position do not justify an adverse conclusion in this case.²⁸⁰

(1) Invading-Presumption

Pursuant to section 23a (1) No. 1(a) paramount market position is deemed to being created or strengthened where a large enterprise having a turnover of at least DM 2 billion enters into a market where small and medium sized companies²⁸¹ have a market share of at least 2/3 and the merging enterprises have a combined market share of at least 5 per cent (*Eindringungsvermutung*).²⁸² The underlying

278 *Emmerich*, Kartellrecht, p. 405.

279 Federal Supreme Court, WuW/E BGH 2231, 2237 (Metro/Kaufhof); Berlin Superior Court, WuW/E OLG 3367, 3382 (Metro/Kaufhof). *Emmerich*, Kartellrecht, p. 406; *Mestmäcker*, in Immenga/Mestmäcker, § 23a, Rn. 7; *Ruppelt*, in Langen/Bunte, § 23a Rn. 18, 19. As to the similar problem concerning sec. 22 (3) No. 1 GWG see Chapter 7.5.1.(1)(b).

280 *Ruppelt*, in Langen/Bunte, § 23a Rn. 17.

281 What is meant by small and medium sized enterprises is not specifically defined in the GWB. It is generally accepted that companies having a turnover of less than DM 50 million are in any case considered small or medium sized. Above that threshold it depends very much on the circumstances, in particular on the volume of the market and the relative size of the remaining competitors. See *Bechtold*, GWB, § 23a, Rn. 7; *Mestmäcker*, in Immenga/Mestmäcker, § 23a, Rn. 24; *Ruppelt*, in Langen/Bunte, § 23a Rn. 6.

282 For an example see Berlin Superior Court, WuW/E OLG 2862, 2867 (Rewe-Florimex) with a discussion of the constitutionality of this provision.

rationale behind this presumption is that a big player entering a market controlled by small and medium sized companies might discourage the smaller firms active in this market and stifle actual and potential competition. Thus, the arguments are broadly in harmony with the *deterrence-doctrine* developed by the courts in connection with the financial strength criterion.²⁸³

(2) Intensifying-Presumption

Under section 23a (1) No. 1(b) a merger is presumed to create or strengthen a paramount market position if an enterprise having a turnover of at least DM 2 billion merges with an enterprise which is market-dominating in at least one market worth at least DM 150 million (*Verstärkungsvermutung*). The philosophy behind this rule is that the combination of financial power (more than DM 2 billion) and market domination must be detrimental to the market concerned. Again, the main line of argument is that of the *deterrence-doctrine*.²⁸⁴ So far, only very few decisions have been based on this provision²⁸⁵ and it appears more than doubtful whether these cases would have been decided in any other way without section 23a (1) No. 1(b).

(3) Giants-Presumption

Independent of the markets on which they are active, under

283 *Emmerich*, Kartellrecht, p. 406.

284 Federal Supreme Court, WuW/E BGH 1501, 1503 (Kfz-Kupplungen); Berlin Superior Court, WuW/E OLG 3137, 3146 (Rheinmetall-WMF). *Bechtold*, GWB, § 23a Rn. 9; *Mestmäcker*, in Immenga/Mestmäcker, GWB, vor § 23a Rn. 29.

285 FCO, WuW/E BKartA 2414, 2417 (WMF-Hutschenreuther); Berlin Superior Court, WuW/E OLG 4865 (WMF-Hutschenreuther).

section 23a (1) No. 2 a merger between two or more “giants” having a combined turnover of at least DM 12 billion with two of the merging enterprises each having a turnover of at least DM 1 billion individually is presumed to create or strengthen a paramount market position (*Gigantenvermutung*).²⁸⁶ Again, the underlying rationale is akin to the arguments put forward in connection with the *financial-resources-criterion* and the *deterrence-doctrine*. However, as the merging enterprises may rebut this presumption by demonstrating that the merger may not be expected to create or strengthen a market-dominating position on the markets where they are active,²⁸⁷ section 23a (1) No. 2 has not often been the basis of the blocking of a merger.²⁸⁸

7.5.3. Countervailing Benefits

The analysis of the substantive merger control criteria has thus far concentrated on the first part of section 24 (1) GWB (and the pertaining presumptions) which provides that a merger creating or strengthening a dominant market position is to be prohibited. However, section 24 (1) GWB goes on to stipulate that a merger fulfilling these preconditions may exceptionally not be blocked if

“the participating enterprises demonstrate that, by means of the merger, improvements of the competitive conditions will also occur and

286 Concerning joint ventures, this presumption applies only if the joint venture is active on a market with a volume of at least DM 750 million. This qualification is made in order not to hamper research- and development-intensive new projects in new developing markets with a relatively low volume which can often only be done by financially very powerful enterprises.

287 For an example see FCO, WuW/E BKartA 2060 (Metro/Kaufhof); Berlin Superior Court, WuW/E OLG 3367, 3382 (Metro/Kaufhof). The Federal Supreme Court, WuW/E BGH 2231, 2237 (Metro/Kaufhof) later quashed these decisions for other reasons (market definition).

288 *Emmerich*, Kartellrecht, p. 408; *Mestmäcker*, in Immenga/Mestmäcker, § 23a Rn. 36. See however, the *Daimler-Benz/MBB* case FCO, WuW/E BKartA 2356.

that these improvements will outweigh the disadvantages of the market domination."

This so-called balancing-clause (Abwägungsklausel) has a parallel in principle in the MMC practice to cautiously take countervailing benefits into account.²⁸⁹ As one would think, what differs are the beneficial factors which are taken into consideration at this stage. While the U.K. merger control authorities are at liberty to pay attention to any public interest benefits, which may include, inter alia, increased efficiency, increased international competitiveness, the rescue of a failing firm, or even environmental advantages, the FCO and the courts in Germany are much more restricted. They may take into account only those structural factors applicable in the assessment of a dominant market position, i.e. the market share, financial resources, access to supply or sales markets, barriers to market entry, countervailing purchasing power, etc. Wider public interest matters, like employment, the rescue of a failing firm, regional development, international competitiveness, and so forth may not be considered by the FCO and the courts.²⁹⁰ These "*overall economic advantages*" and "*overriding public interest*" issues are according to section 24 (3) GWB, because of the inherent political element involved, exclusively reserved for the Federal Minister of Economics as discussed above.²⁹¹ The possible competition benefits flowing from a merger may (logically) not be found on the very market concerning which the FCO has come to the conclusion that a dominant position is created or strengthened. The countervailing benefits may only be located on neighbouring or third markets and offset the competitive detriments in the market where the dominant position is created or strengthened.²⁹² For example, a

289 See Chapter 6.4.3. at pp. 262 with further references.

290 Bechtold, GWB, § 24 Rn. 17; Mestmäcker, in Immenga/Mestmäcker, § 24 Rn. 179; Ruppelt, in Langen/Bunte, § 24 Rn. 47.

291 Chapter 7.4.2. at pp. 311.

292 See very clearly Ruppelt, in Langen/Bunte, § 24 Rn. 48, 49 and Mestmäcker, in Immenga/Mestmäcker, § 24 Rn. 181-183. It is sometimes said that the countervailing competitive improvements which the parties may demonstrate may also be discovered on the very market

merger between two diversified companies may strengthen a market-dominating position in the market for the X-product leading to an adverse finding by the FCO. At the same time the very merger may lead to competitive improvements in a different market for, say, the Y-product in that the market leader in the Y-market is now challenged by the merging enterprises. In that sort of cross-situation, the merging enterprises may try to demonstrate that the improvements in the Y-market outweigh the competitive detriments in the X-market.

Contrary to the general rule, concerning these outweighing third-market competitive improvements, the wording of section 24 (1) GWB leaves no doubt that the burden of proof lies with the merging enterprises. The standard of proof required of the enterprises is high: They have to demonstrate not only that the claimed improvements are highly likely to occur, but also that the improvements could not be achieved by a less anti-competitive means than the merger.²⁹³ Given the high standard of proof required, the FCO and the courts are usually sceptical that (only) the anti-competitive merger would yield third-market benefits of sufficient magnitude to *outweigh* the adverse effects. The balancing clause has therefore been of very limited practical relevance, at least in recent years.²⁹⁴

concerning which the FCO has found a market dominating position (*Bechtold*, GWB, § 24 Rn. 20; *Heidenhain/Schneider*, German Antitrust Law, para 348; *Harms*, in GK, § 24 Rn. 631). This opinion, however, appears not to be in line with the logic of the law. As the FCO has in making its judgement to take into account both beneficial and detrimental effects on that market anyway, only benefits on third markets can be meant.

293 Federal Supreme Court, WuW/E BGH 1533, 1539 (Erdgas Schwaben). FCO WuW/E BKartA 1582 (Kaiser/VAW); Berlin Superior Court, WuW/E KG 3759, 3767 (Pillsbury/Sonnen-Bassermann); Berlin Superior Court, WuW/E KG 3767, 3773 (Niederrheinische Anzeigenblätter) and Federal Supreme Court, WuW/E BGH 2425, 2431 (Niederrheinische Anzeigenblätter).

294 *Emmerich*, Kartellrecht, p. 416; *Markert*, Merger Control in Germany: Substantive Aspects, Fordham 1990, p. 149, 150. For examples see FCO, WuW/E BKartA 1650 (Erdgas Schwaben); Berlin Superior Court, WuW/E OLG 1900 (Erdgas Schwaben); Federal Supreme Court, WuW/E BGH 1533, 1539 (Erdgas Schwaben); Federal Supreme Court, WuW/E BGH 2899, 2902 (Panorama-Anzeigenblätter).

7.6. Concluding Remarks

Apart from of course numerous details, it has been demonstrated that there are a number of fundamental - almost cultural - differences between merger control in Britain and Germany regarding both procedural and substantive law.

As to procedural aspects, the comparison between the regulatory authorities involved has revealed the contrasting concepts concerning the nature of merger control law. Being of a distinctly administrative nature in Germany with the anyway limited role of the Federal Minister of Economics more and more falling into oblivion, in Britain merger control contains a political element and is to some extent seen as means to shape industrial policy, which is why only the Secretary of State may block a merger. Moreover, the overriding legal values of the merger control process in Germany are independence and predictability, which is not to the same degree true for Britain, where it appears that co-operation with business and industry and flexibility are higher valued than in Germany. The comparison between the status and background of the members of the British MMC on the one hand and members of the decisions-units of the FCO on the other hand exemplifies this more general point. In a sense, merger control in Germany is also more confrontational as the heavy involvement of the courts indicates. There has been hardly any blocking order by the FCO which was not subsequently challenged in court. The opposite is true for Britain.

The British lust for flexibility versus the German desire for predictability is also reflected in the substantive merger control law. This is most evident with respect to the appraisal criteria. British law being based on the comprehensive *public interest* concept which allows the merger control authorities “to take into account all matters

which appear to them in the particular circumstances to be relevant"²⁹⁵ is necessarily much more flexible than German law which focuses strictly on the question whether a *market-dominating position* has arisen or is being strengthened. The difference between British and German law is further increased by the existence of legal presumptions in the GWB. Although it has been demonstrated that the presumptions are in practice relatively harmless as the FCO and the courts treat them with suspicion, they still are a factor to be taken into account. This is particularly true for section 22 (3) GWB, the market-share presumption. Broadly speaking, the market share criterion followed by the financial strength criterion (deterrence-doctrine) are the factors of predominant importance in assessing market domination.

295 Sec. 84 (1) FTA 1973.

Chapter 8

EUROPEAN MERGER CONTROL

8.1. Introduction

There exist at present eleven national merger control systems within the European Community,¹ two of which have been examined in the previous chapters. Needless to say, cross-border mergers and acquisitions within Europe are not made any easier by this regulatory environment. Companies effecting transnational acquisitions may have to deal with different national authorities, multiple filing requirements and deadlines, and the substantive merger control law may also differ substantially as is the case with Britain and Germany. The EC-Commission is aware of about one hundred cross-border acquisitions where multiple notifications to different national merger control authorities were required within the last two and half years.² Though probably lucrative for legal advisers, for the participating companies this is not only costly and time-consuming, but may also lead to conflicting decisions by the different national authorities involved. Moreover, a national authority may not be able to properly assess a cross-border merger as its perspective is inevitably mainly confined to the national market whereas in reality geographic markets often exceed national borders.

Pursuant to Article 3 of the EC-Treaty, which requires “a system

1 *EC-Commission, Green Paper on the Review of the Merger Regulation, COM (96) 19 final, para 14.*

2 *EC-Commission, Green Paper on the Review of the Merger Regulation, 1996, para 87.*

ensuring that competition in the internal market is not distorted", and in order to remedy the somewhat unsatisfying regulatory state of affairs within the common market described above at least to some extent, the EC-Council adopted following more than 16 years of debate on 21 December 1989 "*Council Regulation 4064/89 on the control of concentrations between undertakings*" (Merger Regulation) which entered into force on 21 September 1990.³

The Merger Regulation basically applies to "*concentrations*" having a "*community dimension*". Its purpose is to cover those mergers causing significant structural changes "*the impact of which on the market goes beyond the national borders of any one Member State.*"⁴ Following the so-called "*one-stop shop*" principle, a concentration falling within the scope of the Merger Regulation may not be assessed by any national competition authority. Control over these mergers lies exclusively with the European Commission. Hence, conflicting decisions are avoided and companies have to deal with only one authority, and only one regulatory framework applies. Concentrations not having a *community dimension*, however, remain subject to national merger control.

8.1.1. Historical Development

The EC-Treaty of Rome, agreed in 1957, did not contain any specific provisions on merger control.⁵ Title III, Chapter 1

3 Council Regulation 4064/98 of December 21, 1989 on the control of concentrations between undertakings, [1990] O.J. L 257/14. An up to date version of the Merger Regulation, pertinent legislation, and numerous complete lists of Commission Decisions can be found in *Jones/Van der Woude/Lewis*, E.C. Competition Law Handbook, 1996.

4 Recital 9 of the Preamble of the Regulation.

5 It should be noted, however, that the ECSC-Treaty of Paris of 1951 granted merger control powers regarding the coal and steel industry to *EC-Commission* (Article 66 of the ECSC-Treaty). However, these provisions cannot be seen as a competition-based merger control system. They were rather aimed at controlling an industry of considerable military importance. See *Löffler*, in *Langen/Bunte*, Kartellrecht, Vorbemerkung zur

(Competition Policy) of the EC-Treaty only regulated restrictive practices (Article 85) and the abuse of power by undertakings having a dominant position within the common market (Article 86). The absence of a comprehensive regulatory merger control framework is not surprising given that at that time, viz 1957, the need for a legal control of mergers, as it is generally accepted nowadays, was not even recognised on a national level let alone on the supra-national European level:⁶ Britain introduced a regulatory system of merger control in 1965,⁷ Germany in 1973,⁸ and France in 1977.⁹ Remarkably, even in 1989 when the European Merger Regulation was finally adopted, apart from Britain, Germany, and France, Portugal and Ireland were the only other EC-Member States with a national merger control law.¹⁰

Yet, the EC-Commission soon discovered its desire to regulate mergers. In 1966 a "*Memorandum on the problem of mergers in the Common Market*" dealing with the question of whether Article 85 EC-Treaty could be used as a tool to control concentrations was published.¹¹ The discussion on European merger control picked up momentum when the Commission in 1971 in the *Continental Can* case courageously applied Article 86 EC-Treaty to a merger, a decision that was subsequently upheld by the European Court of

FKVO 4064/89, Rn. 2. For a detailed discussion of merger control under the ECSC-Treaty see *Bos/Stuyck/Wytinck*, Concentration Control in the EEC, Chapter 2.

6 See *Jones/González-Díaz*, The EEC Merger Regulation, p. 83 who point out that in the 1950s and 1960s mergers were welcomed without exception as a means to enabling European companies to compete effectively with the very large U.S. corporations.

7 See Chapter 6.1.1. at pp. 206.

8 See Chapter 7.1.1. at pp. 266.

9 *Löffler*, in *Langen/Bunte*, Kartellrecht, Vorbemerkung zur FKVO 4064/89, Rn. 4.

10 *Löffler*, in *Langen/Bunte*, Kartellrecht, Vorbemerkung zur FKVO 4064/89, Rn. 6.

11 *EC-Commission*, Memorandum on the problem of merger in the Common Market, Competition Series Study No. 3, Brussels 1966. Part III of the memorandum is reproduced in *Ritter/Rawlinson/Braun*, EEC Competition Law, Appendix 20.

Justice.¹² However, the Commission never really doubted that under Article 85 and Article 86 EC-Treaty the merger control exercisable was at best fragmentary.¹³ Hence, it became clear relatively early on that the best legal way to deal with mergers on European level would be by way of a directly binding regulation establishing a single authority charged with supervising European mergers.¹⁴

Eventually, in 1973 the Commission published its first proposal for a Regulation on the control of concentrations.¹⁵ As one would expect, the proposal met with considerable controversy, the main points of debate being the legal basis of the proposed regulation (Article 87 and/or Article 235 of the EC-Treaty), the separation of power between the Member States and the European institutions, and on European level the division of power between the Council and the Commission. In the years to come, a number of amendments to the 1973 proposal were made,¹⁶ but the overall impression is that the Merger Regulation was not seen as a high priority measure either by the Commission or the Member States.¹⁷ This changed when Commissioner *Peter Sutherland* presented two new proposals in 1988 and 1989 respectively.¹⁸ The European Court of Justice again added momentum to the discussion when it suggested in the famous *Philip Morris* case¹⁹ that Article 85 of the

12 *Europemballage and Continental Can v. Commission*, Case 6/72, [1973] ECR 215. For a detailed discussion see *Downes/Ellison*, The legal control of mergers in the EC, pp. 3 and *Ritter/Rawlinson/Braun*, EEC Competition Law, pp. 333.

13 As to Article 85 and Article 86 see Chapter 8.1.2. at pp. 339.

14 See Art. 189 of the EC-Treaty.

15 Proposal for a Regulation (EEC) of the Council on the control of concentration between undertakings, [1973] O.J. C 92/1.

16 For a complete list of all amendments and other Brussels-publications on the issue see *Löffler*, in *Langen/Bunte*, Kartellrecht, Vorbemerkung zur FKVO 4064/89, Rn. 9.

17 See *Bos/Stuyck/Wytinck*, Concentration Control in the EEC, p. 121.

18 Amended Proposal for a Council Regulation (EEC) on the control of concentrations between undertakings, 25 April 1988, [1988] O.J. C 130/4. Amended Proposal for a Council Regulation (EEC) on the control of concentrations between undertakings, 30 November 1988, [1989] O.J. C 22/14.

19 *BAT and RJ Reynolds v. Commission*, Cases 142 & 156/84, [1987] ECR 4487. For a detailed discussion see *Downes/Ellison*, The legal control of mergers in the EC, pp. 18.

EC-Treaty might in the absence of any other European merger control provisions be applicable to certain mergers: a result which nobody wanted as merger control under Article 85 of the EC-Treaty would have been both rigorous and fragmentary. After intense negotiations the European Merger Regulation was finally adopted in December 1989 and entered into force on 21 September 1990. Given that an unanimous Council vote was required for its adoption,²⁰ it is not surprising that the Regulation bears the signs of political compromise, in particular with respect to the division of powers between the Commission and the Member States.²¹ Prominent examples of this compromise are the definition of the *community dimension* (turnover thresholds)²² required for the Regulation to be applicable and the so-called "*German clause*"²³ concerning the referral from the Commission to a Member State. Following its legal obligation²⁴ to review the turnover thresholds and the referral rules, the Commission recently published, in January 1996, a "*Green Paper on the Review of the Merger Regulation*".²⁵ The suggestions made there will be discussed where appropriate.²⁶

8.1.2. Residual Applicability of Articles 85 and 86 EC-Treaty

A difficult legal question is the applicability of Articles 85 and 86 EC-Treaty to concentrations after the entry into force of the Merger Regulation. Articles 85 and 86 of the EC-Treaty are primary EC-

20 As the Regulation is now based jointly on Art. 87 and Art. 235 of the EC-Treaty, the latter of which requires an unanimous vote.

21 *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, para 46; *Löffler*, in *Langen/Bunte*, Kartellrecht, Art 1 FKVO, Rn. 7.

22 Art. 1. See Chapter 8.3.2. at pp. 362.

23 Art. 9. See Chapter 8.3.3.(1) at pp. 370.

24 See Art. 1(3), 9(5), 22 of the Regulation.

25 *EC-Commission*, Community Merger Control, Green Paper on the Review of the Merger Regulation, COM(96) 19 final, Brussels, 31 January 1996.

26 See Chapter 8.3.2.(4) at pp. 367.

legislation. The Merger Regulation is secondary legislation. Hence, the latter ranks lower in the hierarchy of European laws and may, thus, not abrogate anything written in the Articles of the EC-Treaty. Consequently, Articles 85 and 86 are legally unaffected by the introduction of the Merger Regulation and the case law as outlined by the European Court of Justice in *Continental Can*²⁷ and *Philip Morris*²⁸ is theoretically still of relevance. In practice, however, the European Commission no longer applies Articles 85 and 86 EC-Treaty to concentrations as defined by Article 3 of the Merger Regulation since its introduction.²⁹ As *Christopher Jones*, who is an Assistant Director General for Competition at the Directorate General IV of the European Commission in Brussels, states "*the potential scope of application of Articles 85 and 86 to concentrations is largely - but not entirely - of historical interest.*"³⁰ In the light of this statement and the fact that Articles 85 and 86 have not been applied to any concentration since the entry into force of the Merger Regulation, the issue will not be discussed any further here.³¹

8.1.3. Statistics

According to the recently published "*Green Paper on the Review of the Merger Regulation*", as of October 1995, 376 concentrations

27 *Europemballage and Continental Can v. Commission*, Case 6/72, [1973] ECR 215.

28 *BAT and RJ Reynolds v. Commission*, Cases 142 & 156/84, [1987] ECR 4487.

29 See however Art. 22(2) of the Merger Regulation which intends to make it procedurally very difficult to apply Art 85, 86 EC-Treaty to concentrations as defined in Art. 3 of the Merger Regulation.

30 *Jones/González-Díaz*, *The EEC Merger Regulation*, p. 79.

31 For a more detailed discussion see *Bos/Stuyck/Wytinck*, *Concentration Control in the EEC*, paras 3-001 et seq.; *Downes/Ellison*, *The legal control of mergers in the EC*, pp. 2 and 178 et seq.; *Fine*, *Mergers and Joint Ventures in Europe*, Chapters 2 and 3; *Jones/González-Díaz*, *The EEC Merger Regulation*, pp. 79; *Ritter/Rawlinson/Braun*, *EEC Competition Law*, pp. 333. For an in-depth analysis in German see: *Kurz*, *Das Verhältnis der EG-Fusionskontrollverordnung zu Artikel 85 und 86 des EWG-Vertrages*, 1993.

had been notified to the Commission, 357 of which resulted in a final decision. Only four concentrations, the last three of which concerned media markets, have been prohibited since the entry into force of the Regulation in September 1990.³² The Commission states that a further 24 transactions were substantially altered so as to take account of the Commission's competition concerns. As of the end of 1995 seven of the Commission's merger decisions have been challenged before the European Courts, of which in four cases the Commission's decisions was upheld³³ while the three remaining cases³⁴ are pending.³⁵ Given these figures it is safe to say that the direct practical impact of the Merger Regulation at least in terms of prohibitions (4) has been comparatively limited.³⁶

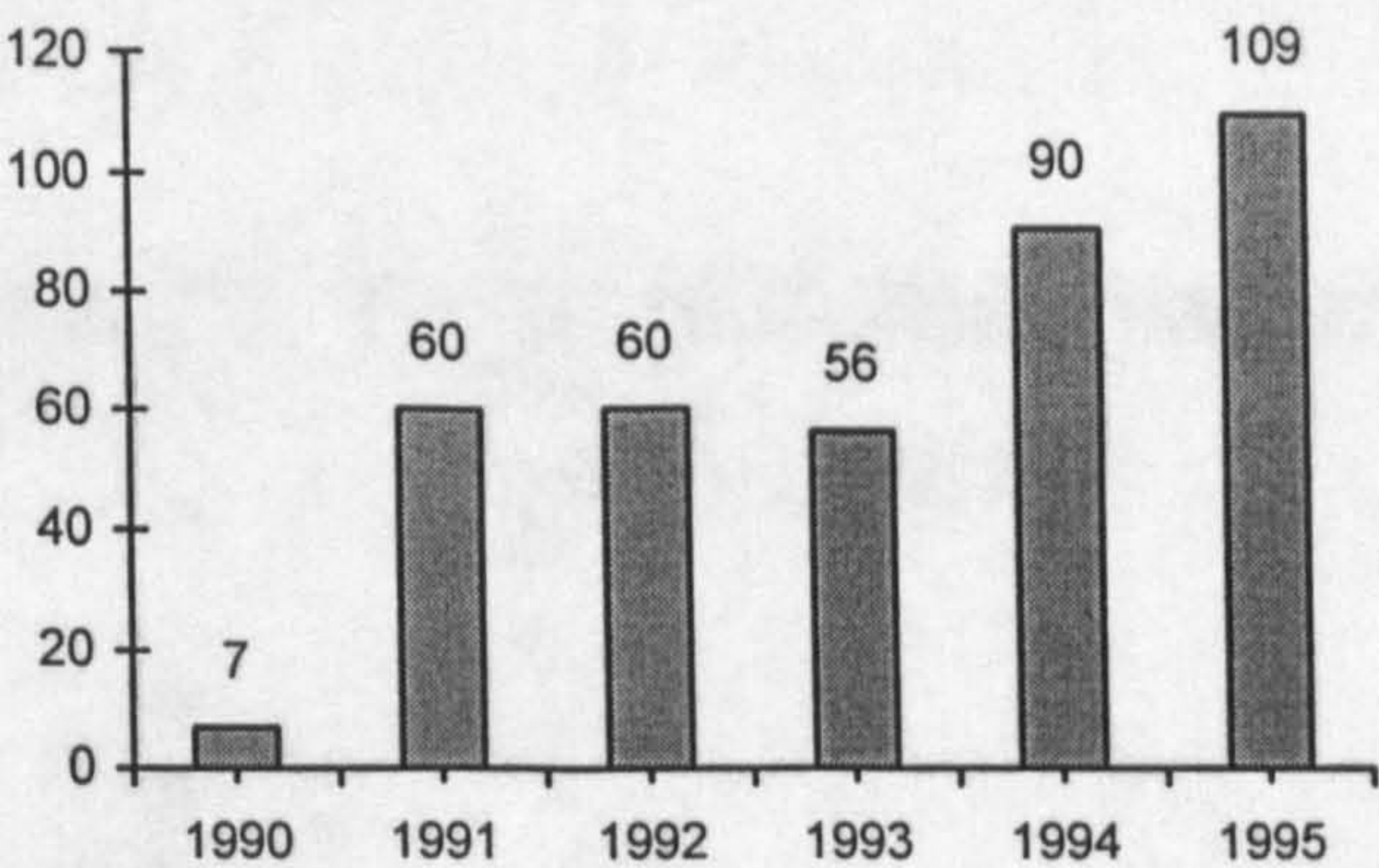
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- 32 Aérospatiale-Alenia/de Havilland, [1991] O.J. L 334/42; MSG Media Service, [1994] O.J. L 364/1; Nordic Satellite Distribution, [1996] O.J. L 53/10; RTL/Veronica/Endemol, [1996] O.J. L 134/33.
- 33 Mediobanca/Generali, [1991] O.J. C 334/23 = CMLR 4 [1992] 81 (Court of First Instance, 28.10.93, case T-83/92; ECJ 11.2.96, case C 480/93); Nestlé/Perrier, [1992] O.J. L 356/1 (Court of First Instance, 27.4.1995, case T-96/92); British Airways/TAT, [1992] O.J. C 326/19 = CMLR 4 [1993] 7 (Court of First Instance, 24.3.1995, case T-3/93).
- 34 Kali+Salz/MdK/Treuhand, [1994] O.J. L 186/38 (ECJ cases C-68/94 and C-38/95); Procter+Gamble/VP Schickedanz, [1994] O.J. L 354/32 (Court of First Instance case T- 290/94); Shell/Montecatini, [1994] O.J. L 332/48 (Court of First Instance case T-322/94).
- 35 Information provided by *Löffler*, who is an FCO official, in *Löffler*, Statistik der EG-Fusionskontrollverfahren nach fünfjähriger Anwendungspraxis, WuW 1996, 209, 212. For discussion of judicial review aspects see *Brown*, Judicial review of Commission Decisions under the Merger Regulation: The First Cases, [1994] 6 ECLR 296-305.
- 36 *Emmerich*, Kartellrecht, p. 339.

Table 18: Decisions under the Merger Regulation

Merger Decisions (Sep. 1990 to Oct. 1995)	Provision	Number
Outside the scope of the Regulation	Art. 6(1)(a)	31
Compatible with the Common Market (first phase)	Art. 6(1)(b)	303
Compatible with the Common Market (second phase)	Art. 8(2)	19
Prohibitions	Art. 8(3)	4

Source: Green Paper on Merger Control, COM(96) 19 final

Table 19: Annual Number of Merger Decisions³⁷



37

Source: DG IV, Die Wettbewerbspolitik der EG 1995, XXV. Bericht.

Table 20: Types of Concentrations 1990-1995³⁸

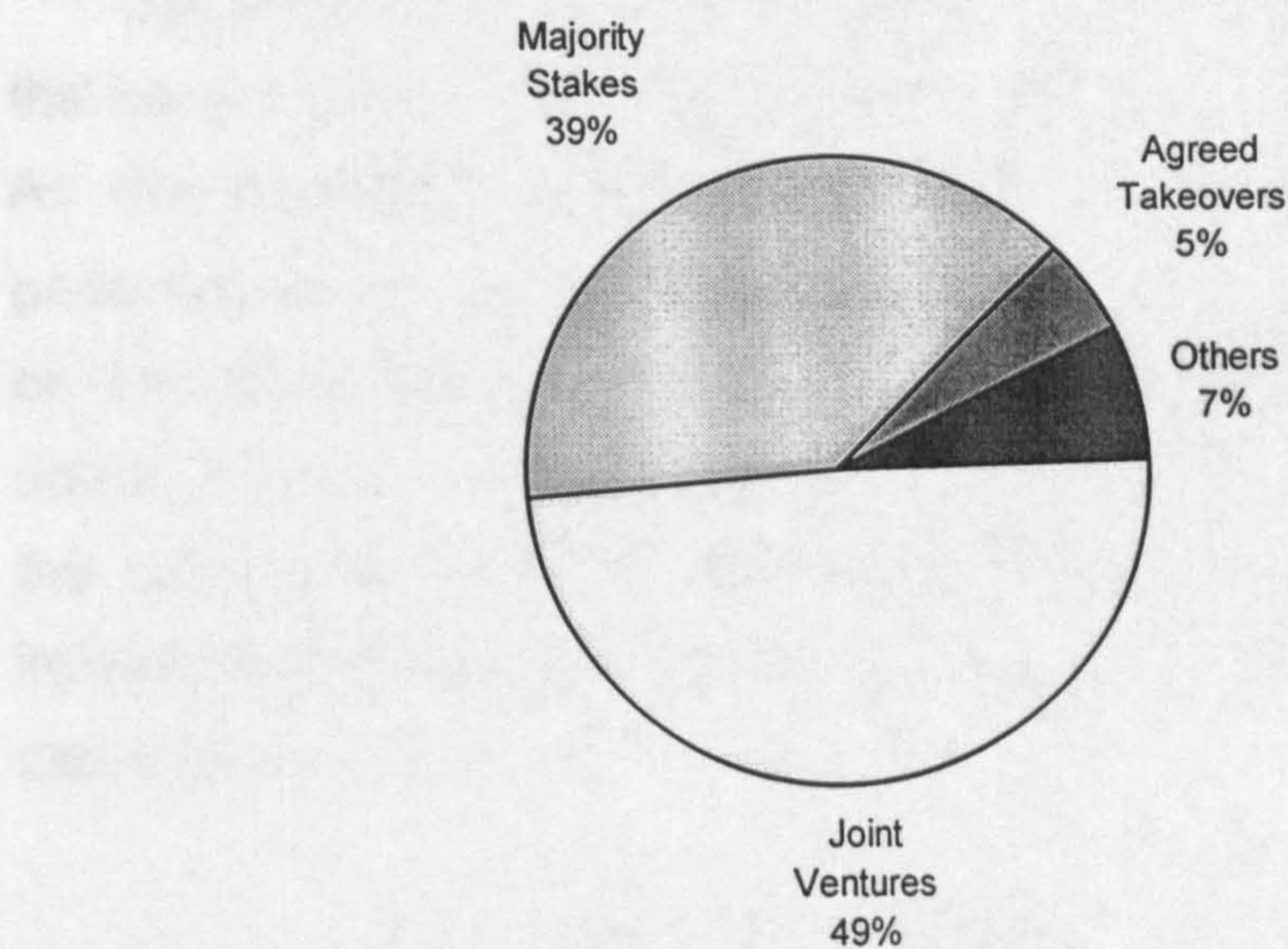
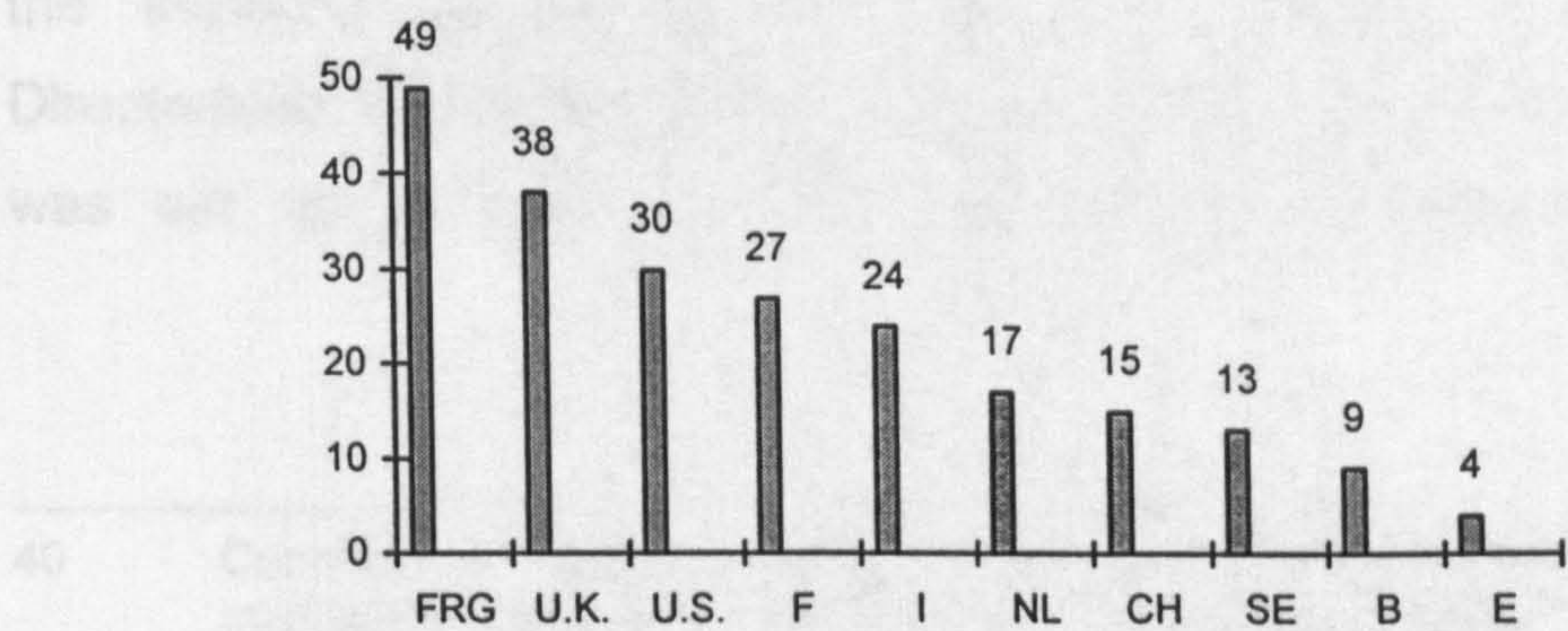


Table 21: Origin of Companies involved
1990-1995³⁹



38 Source: DG IV, Die Wettbewerbspolitik der EG 1995, XXV. Bericht.
39 Source: DG IV, Die Wettbewerbspolitik der EG 1995, XXV. Bericht.

8.2. Overview over the Merger Control Process

The purpose of this subchapter is to provide an overview over the merger control institutions and the procedure at European level. As the procedural aspects of the Merger Regulation and the pertaining Implementing Regulation,⁴⁰ which contains further details on the procedure, are generally considered successful, there is unlike in Britain relatively little debate concerning these issues with the notable exception of recently intensified (German) calls for an independent European Cartel Office modelled on the Federal Cartel Office in Berlin.⁴¹

8.2.1. Institutional Framework

The Competition Directorate-General of the European Commission (DG IV) is charged with the enforcement of the competition rules under the EC-Treaty, the Merger Regulation and the Implementing Regulation.⁴² DG IV is divided into seven Directorates. Directorate B, the so-called *Merger Task Force*, which was set up in 1990 by Sir Leon Brittain, Commissioner for

40 Commission Regulation (E.C.) No. 3384/94 of December 21, 1994 on the notifications, time limits and hearings provided for in Council Regulation (EEC) No. 4064/89 on the control of concentrations between undertakings [1994] O.J. L 377/1.

41 See *Financial Times* and *Frankfurter Allgemeine Zeitung* of May 31, 1996. Also Groger/Janicki, *Weiterentwicklung des Europäischen Wettbewerbsrechts*, WuW 1992, 991, 1001. As to details see Chapter 8.2.1. at pp. 344.

42 An up to date DG IV staff list including phone-number can be found in the "*Competition Policy Newsletter*" which is published quarterly by the Competition Directorate General of the European Commission.

Competition at that time, handles concentrations.⁴³

The Merger Task Force consists of a multinational, multidisciplinary group of about 50 members, around half of whom are senior civil servants (mostly lawyers and economists), and half of those are on secondment, normally for a three-year term, from national competition authorities.⁴⁴ It is headed by a Director and further divided into four operational units, each of which is guided by a Head of Unit. These units are unlike the decision-units of the German FCO not organized on a sectorial basis.⁴⁵ Neither are they dependent and charged with the final decision-making.

Once the Merger Task Force has been contacted either formally via a notification or informally, a “case team” is set up immediately on an ad hoc basis. It is headed by a “case manager”, usually one of the Heads of Unit, and at least two “case handlers” who are chosen on the basis of expertise and language.⁴⁶ At that stage the European procedure bears a resemblance to the MMC procedure.⁴⁷

43 Address: European Commission, Merger Task Force, Avenue de Cortenberg 150, B-1040 Brussels, Tel. (32-2) 295.86.81, Fax. (32-2) 296.43.01.

44 *Drauz/Schröder*, *Praxis der Fusionskontrolle*, p. 186; See also with slightly different numbers *Krause*, E.C. Merger Control: An outside view from inside the Merger Task Force, [1995] J.B.L. 627, 628.

45 See *Competition Policy Newsletter*, DG IV staff list. *Fine*, *Mergers and Joint Ventures in Europe*, para 5-003. Slightly critical of this aspect *Drauz/Schröder*, *Praxis der europäischen Fusionskontrolle*, p. 186, because managers and their advisers do not know beforehand who is going to handle their case. However, a positive aspect of this regulatory detail appears to be that the scope for lobbying (or more) is reduced this way.

46 For a description of the Merger Task Force's day-to-day work see *Krause*, E.C. Merger Control: An outside view from inside the Merger Task Force, [1995] J.B.L. 627-637, who paints an extremely positive picture. Also *Drauz/Schröder*, *Praxis der Fusionskontrolle*, pp. 186; *Fine*, *Mergers and Joint Ventures in Europe*, para 5-003. For a highly critical assessment of the Commission-bureaucracy see *Portwood*, *Mergers under EEC Competition Law*, pp. 101. With respect to case teams *Portwood* points out that this may lead to inconsistencies within the Merger Task Force as certain teams may take a more liberal approach than others (p. 103). However, as those case teams are established on an ad hoc basis for each individual case, the criticism by *Portwood* appears unjustified. Clearly, not all of the 50 members of the Merger Task Force can be involved in handling a case given the strict deadlines imposed by the Merger Regulation.

47 See Chapter 6.3.3.(2) at pp. 235.

The European Commission being a political institution and with the final blocking decisions taken by the college of all Commissioners, there has repeatedly been criticism as to the Commission's alleged susceptibility to political pressure. It has therefore been suggested, in particular by the German Government, and recently by the head of the Italian competition authority, *Mr Giuliano Amato*, that an independent competition authority taking over the Merger Task Force's role should be set up in order to avoid undue political influence.⁴⁸ The calls for an independent European Cartel Office are almost as old as the EC-Treaty itself.⁴⁹ From a German perspective, these proposals are clearly modelled on the German Federal Cartel Office system with its independence and strict focus on competition rather than industrial policy matters. Moreover, the German governmental criticism has to be seen in the wider context of frequent claims that the merger control regime exercised in Brussels was too lenient. This alleged leniency has led to lawyers openly advising their clients to tailor their transactions so as to avoid German law. A Mergers and Acquisitions Handbook published by a major German law firm states, for example: *"In cases of doubt, where there is room for structuring an acquisition, it is preferable for it fall under European rather than German jurisdiction."*⁵⁰ This development is, of course, deplored, by the FCO in Berlin, as *Stefan Held*, its former Vice President made clear: *"...stricter application of national merger control puts 'smaller mergers' at a disadvantage vis-à-vis 'large mergers' that come under EC merger control, which is expected to be more lenient. ... As I see it, the reputation of both the national cartel authorities and the EC-*

48 *Financial Times* and *Frankfurter Allgemeine Zeitung* of May 31, 1996. Also *Groger/Janicki*, *Weiterentwicklung des Europäischen Wettbewerbsrechts*, WuW 1992, 991, 1001.

49 For a detailed analysis of this idea from a German perspective see *Ehlermann*, *Reflections on a European Cartel Office*, [1995] CMLRev 470-486.

50 *Droste (law firm)*, *Mergers & Acquisitions in Germany*, p. 291. See also *Bechtold*, who is one of the leading anti-trust lawyers, in *Antitrust law in*

Commission will be compromised in the long run if the business community view them as rigorous and lenient enforcers respectively and manipulate the issue of jurisdiction at will."⁵¹ As to the British view on these issues, the author is not aware of any claims of European merger control being too lenient or calls for an independent European Cartel Office.

Coming back to the issue of undue political influence on merger decisions, it is indeed difficult to see why all Commissioners including those who are not concerned with competition policy at all should decide on merger cases. After all, competition law is a highly specialized and complex subject which requires not only solid legal knowledge but also a very deep understanding of the economics regarding the markets concerned. Albeit the individual Commissioners may be highly qualified experts in the field of their Directorate General, it seems doubtful whether all of them are experts on competition law and have sufficient expertise and knowledge of the actual cases enabling them to make a well informed decision. This (political) aspect of European merger control differs from both Britain and Germany as these regulatory systems try to ensure that the final merger decisions are taken by experts. In the U.K. the ultimate power to block a merger rests with the Secretary of State for Trade and Industry, who should be an expert, and not the whole cabinet (which would be the equivalent to the full Commission).⁵² In Germany, decisions are taken by the independent full-time members of the decision-units of the FCO and there is no involvement of a political institution at all.⁵³

However, the German and Italian idea of turning DG IV into an independent European competition agency is hardly more than

the European Community and Germany - An uncoordinated co-existence, in Fordham 1992, p. 343, 353.

51 *Held*, in German Antitrust Law and Policy, Fordham 1992, pp. 311, 320 et seq.

52 See Chapter 6.3.2. at pp. 229 and Chapter 6.3.4. at pp. 242.

53 See Chapter 7.4.1. at pp. 304. As to the exceptional involvement of the Federal Minister of Economics see Chapter 7.4.2. at pp. 311.

wishful thinking. With the Merger Task Force at DG IV working smoothly from an administrative point of view and in the absence of any clear evidence as to politically motivated merger decisions,⁵⁴ there is little direct need for any fundamental institutional change in the foreseeable future.⁵⁵ From a political point of view, establishing an independent European Cartel Office would mean that the Member States lose influence which under the present system they have through “*their*” Commissioners. Those Member States which are generally rather sceptical of further European integration can therefore not be expected to be in favour of an independent European competition authority for political reasons. The present Competition Commissioner, *Karel van Miert*, fiercely rejected any ideas as to an independent agency arguing that such an agency would be more costly and controversial, and even more open to political influence from Member States than the Commission presently is.⁵⁶ The establishment of an independent European Cartel Office being politically unrealistic, a more acceptable reform-response to the criticism expressed above could be to strengthen the position of the Competition Commissioner⁵⁷ by way of delegating the decision-making power exclusively to him - quite like in Britain where the power of blocking mergers rests with the Secretary of State of Trade and Industry rather than the whole cabinet.

54 *Ehlermann*, Reflections on a European Cartel Office, [1995] CMLRev 470, 475. An example of political influence cited by *Bishop/Bishop*, Reforming Competition Policy: Bundeskartellamt - Model or Muddle?, [1996] 4 ECLR 207, seems to be *Mannesmann/Vallourec/Ilva*, [1994] O.J. L 102/15, as this concentration was cleared after the College of Commissioners voted against the advice of the Competition Commissioner.

55 *Bishop/Bishop*, Reforming Competition Policy: Bundeskartellamt - Model or Muddle?, [1996] 4 ECLR 207, 209.

56 Official EC Press Info IP/96/457. Also *Financial Times* and *Frankfurter Allgemeine Zeitung* of May 31, 1996.

57 See also *Ehlermann*, Reflections on a European Cartel Office, [1995] CMLREV 470, 483.

8.2.2. Procedure

As the procedure as handled by the Merger Task Force is generally considered very efficient and effective, a few broad remarks together with the flow chart at page 353 may suffice.⁵⁸

The procedure is basically divided into two stages: Phase 1 and Phase 2. The initial Phase 1 investigation has to be concluded within one month from the receipt of a complete notification as required by *Form CO* and is of a cursory nature.⁵⁹ Both before and within the first three weeks following notification Article 7 of the Merger Regulation prohibits the implementation of concentrations having a *community dimension*. The Commission may decide to extend the suspensory period on its own initiative. According to Article 9 the Commission may refer a notified concentration to the competent authority of a Member State if the concentration affects a distinct market within that particular Member State (German Clause).⁶⁰ Vice versa, under Article 22 (3) a Member State may refer a national merger to the Commission if that merger affects trade between Member States (Dutch Clause).⁶¹ Phase 1 ends with a decision taken by the *Commissioner for Competition* pursuant to Article 6 of the Merger Regulation.⁶² As Table 18 above at page 342 shows the

58 For a detailed description of the procedural aspects see the following books: *Bos/Stuyck/Wytinck*, Concentration Control in the EEC, para 4-157 to 4-382; *Cook/Kerse*, EEC Merger Control, Chapter 5; *Downes/Ellison*, The legal control of mergers in the EC, Chapter 4; *Fine*, Mergers and Joint Ventures in Europe, Chapters 5; *Jones/González-Díaz*, The EEC Merger Regulation, Chapter 15; *Portwood*, Mergers under EEC Competition Law, Chapters 6 and 7. In German see for example: *Drauz/Schröder*, Praxis der europäischen Fusionskontrolle, pp. 186-230. For a commentary on the Merger Regulation see *Löffler*, in *Langen/Bunte*, Kartellrecht, FKVO.

59 Form CO, [1994] O.J. L 377/9. Form CO is an annex to the Merger Regulation 4064/89. Reproduced, e.g., in *Jones/Van der Woude/Lewis*, E.C. Competition Law Handbook, 1996, p. 647.

60 For details see Chapter 8.3.3.(1) at pp. 370.

61 For details see Chapter 8.3.3.(2) at pp. 373.

62 The Merger Regulation only speaks of decisions by "the Commission." However, the Commission's Rules of Procedure ([1967] O.J. L 145/1) in

overwhelming majority of decisions taken by the Commission are Article 6 decisions. As these Phase 1 decisions are not published in full in the Official Journal, Series L, of the EC, there is a certain lack of transparency with regard to these decisions.⁶³ Only a brief notice that a decision has been taken is published in Series C of the Official Journal. Interested parties may, however, obtain a copy from the Merger Task Force. Article 6 decisions may have one of the following tenors, namely

- (1) *to clear the merger because it is not within the scope of the Regulation, Article 6(1)(a).*
- (2) *to clear the merger because it does not raise serious doubts as to its compatibility with the common market, Article 6(1)(b).*
- (3) *to initiate Phase 2 proceedings because the merger raises serious doubts as to its compatibility with the common market, Article 6(1)(c). This decision is taken by the Competition Commissioner in conjunction with the president.*

As Table 18 above at page 342 indicates, far less than 10 per cent of all notified mergers reach Phase 2. Since the entry into force of the Regulation in 1990 until October 1995 only 23 concentrations were subject to a Phase 2 investigation.⁶⁴ In Phase 2, a detailed appraisal of the merger takes place the time-limit being a further four months within which a final decision pursuant to Article 8 has to be reached:

- (1) *Compatible with the common market, Article 8(2), sentence 1.*

their amended form provide for the delegation of powers. For details see *Jones/González-Díaz, The EEC Merger Regulation*, p. 222.

63 However, press notices are published and summaries of the decisions are often published in competition law journals like *Common Market Law Review* or *Wirtschaft und Wettbewerb* (WuW). Not quite up-to date, but a collection of merger decisions (translated into English) can be found in Gijlstra (editor), *Competition Law in Western Europe and the USA*, European Communities Materials, Volume B14 (looseleaf).

64 See Table 18 at p. 342 above.

- (2) *Compatible with the common market, but modifications (conditions, obligations) required, Article 8(2), sentence 2.*
- (3) *Incompatible with the common market, Article 8(3). The Commission may, if necessary,⁶⁵ order the dissolution of the concentration or require any other appropriate measures to remedy the anti-competitive effects.*

Phase 2 decisions must be taken by the *full Commission*.⁶⁶ Article 19 of the Merger Regulation furthermore requires that the Commission carries out all procedures in close and constant liaison with the competent authorities of the Member States. In particular, an Advisory Committee consisting of representatives of the authorities of the Member States is to be consulted before any Article 8 decision is taken.⁶⁷ It appears conceivable that through this route a political element may come into play. Following an adverse decision, the parties have two months to lodge an appeal with the European Court of First Instance.⁶⁸ Unlike Article 6 decisions, Article 8 decisions are to be published in their full (translated) version in the Official Journal, Series L, of the EC. Hence, with respect to these decisions a high degree of transparency is ensured, although it

65 This was necessary only once: *RTL/Veronica/Endemol*, [1996] O.J. L 134/33 para 116. Under the Merger Regulation, concentrations are suspended until cleared. Hence, there will not normally be a need for a dissolution-order. In *RTL/Veronica/Endemol*, however, the need arose because this was not a "European" case, but a case referred to the Commission by the Netherlands under the "Dutch Clause", Art. 22. As to the Dutch Clause see Chapter 8.3.3.(2) at pp. 373.

66 *Fine*, Mergers and Joint Ventures in Europe, para 5-058; *Jones/González-Díaz*, The EEC Merger Regulation, p. 222. As to criticism see above Chapter 8.2.1. at pp. 344.

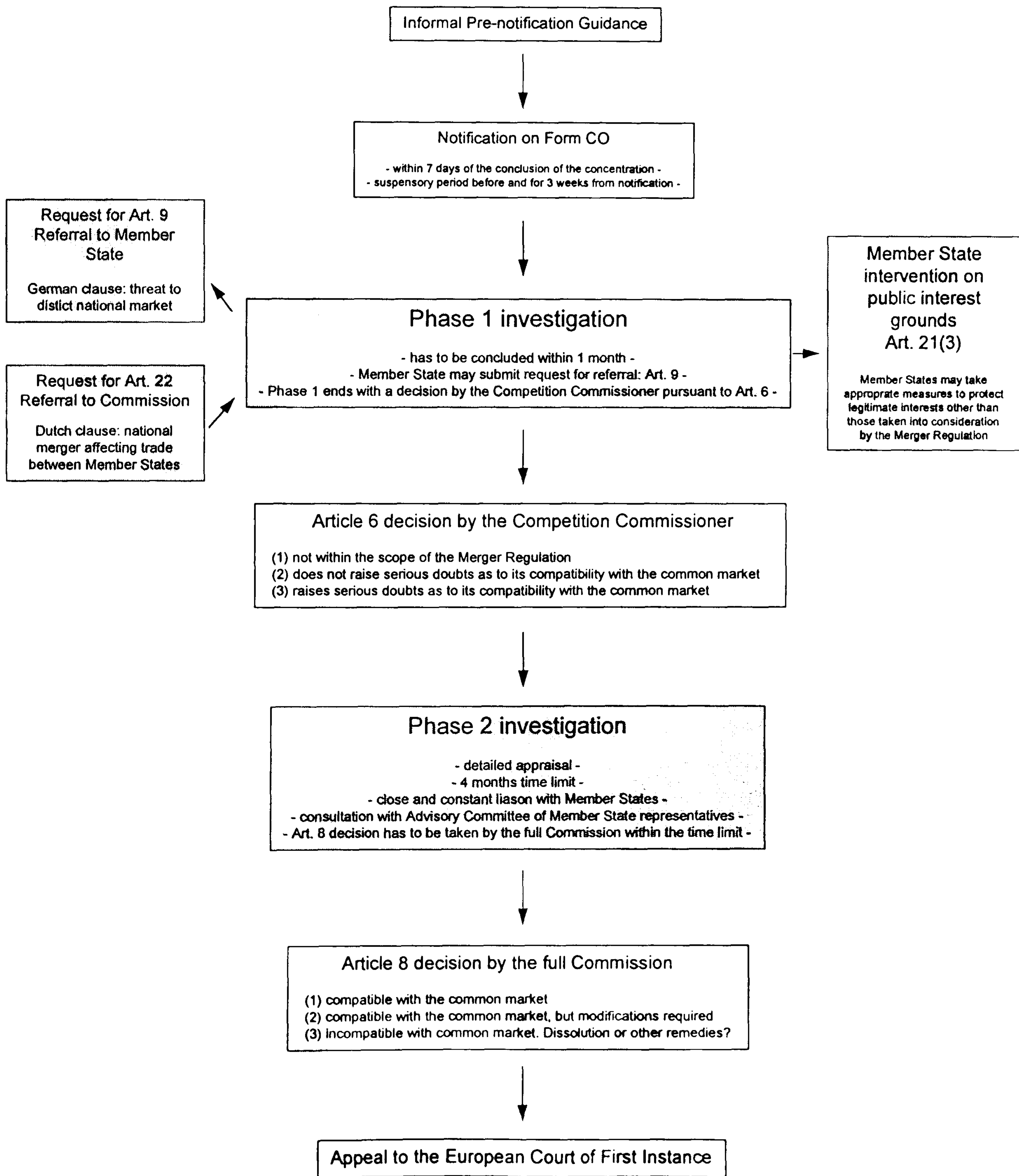
67 Art. 19 (3) to (7) of the Merger Regulation. For a more detailed analysis see *Bos/Stuyck/Wytinck*, Concentration Control in the EEC, paras 4-310 et seq.

68 The Merger Regulation itself only refers only to the European Court of Justice. However, Council Decision 88/591 which established the Court of First Instance of the European Communities ([1987] O.J. L 169/1) stipulates that actions under Article 173 of the EC-Treaty brought by natural or legal persons against Decisions of the Commission are to be considered by the European Court of First Instance. For further details see *Bos/Stuyck/Wytinck*, Concentration Control in the EEC, paras 4-350 et seq.; *Fine*, Mergers and Joint Ventures in Europe, paras 5-062 et seq; *Portwood*, Mergers under EEC Competition Law, pp. 158.

often takes several months for the decisions to be finally published in the Official Journal.⁶⁹

69 Take for example the two latest prohibitions: The decision in *Nordic Satellite Distribution* was taken July 19, 1996 and published in the O.J. on March 2, 1996 (L 53/21). In *RTL/Veronica/Endemol* the concentration was blocked on September 20, 1995, the decision was published on June 6, 1996 (L 134/33).

Merger Task Force Procedure



8.3. Jurisdiction

The Merger Regulation being a supra-national set of rules, the demarcation between Community and national sovereignty over mergers is of crucial importance.⁷⁰ Clear and simple rules appear particularly desirable in order to avoid jurisdictional conflicts between the Commission and national authorities over merger cases. By and large, the jurisdictional test applied by the Merger Regulation lives up to these expectations. The first paragraph of Article 21 (2) of the Merger Regulation states in pursuance of the one-stop shop principle that “*no Member State shall apply its national legislation on competition to any concentration that has a Community dimension.*”⁷¹ Hence, the jurisdictional reach of the Regulation is defined through the terms “*concentration*” and “*Community dimension*”. What is meant by these terms will be discussed in subchapters 8.3.1.⁷² and 8.3.2.⁷³ respectively.

The two-part jurisdictional test outlined above is refined by three exceptions to the general rule that concentrations having a *community dimension* are exclusively assessed by the Commission and, vice versa, those not having a *community dimension* are investigated on Member State level only. These jurisdictional exceptions are examined in subchapter 8.3.3.⁷⁴

70 As to the competition rules applying in the European Economic Area (EEA) under Article 57 of the EEA-Agreement see *Broberg*, The Delimitation of Jurisdiction with regard to Concentration Control under the EEA Agreement, [1995] 1 ECLR 30-39.

71 This rule, however, is subject to the exceptions discussed in Chapter 8.3.3. at pp. 370.

72 See pp. 370.

73 See pp. 373.

74 See pp. 375.

8.3.1. Definition of a Concentration

According to Article 3 (1) a concentration is deemed to arise where (a) two or more undertakings *merge*, or (b) two or more persons⁷⁵ or undertakings *acquire control* of another undertaking.⁷⁶ Hence, the Regulation differentiates between two types of transactions: (technical) mergers on the one hand and the acquisition of sole or joint control on the other.⁷⁷ This approach differs from both British and German law. While the British Fair Trading Act 1973 does not attempt to describe any specific transactions at all, but uses the concept of enterprises ceasing to be distinct enterprises,⁷⁸ the German GWB tries, at least in principle, to enumerate and describe specific transactions constituting mergers exhaustively.⁷⁹

(1) Mergers

The regulation does not provide a definition of the phrase “*two or more independent enterprises merge*.” Yet, a direction comparison between Article 3 (1) (a) and Article 3 (1) (b) has led the to the generally accepted opinion that subsection (a) is intended to cover amalgamations (fusions) in which two or more companies are amalgamated into one company, whereas the much broader

75 Only persons already controlling at least one undertaking are covered by the Regulation, Art. 3 (1)(b) of the Regulation.

76 Art. 3 (5) provides for a number of exceptions regarding certain transactions, e.g. temporary holdings by banks and insurance companies.

77 In order to provide guidance as to how the Commission interprets the notion of a concentration, the Commission has published a “Notice on the notion of a concentration under Council Regulation (EEC) No. 4064/89: see [1994] O.J. C 385/5. Reproduced in *Jones/Van der Woude/Lewis*, E.C. Competition Law Handbook, 1996, pp. 670.

78 See Chapter 6.2.1. at pp. 214.

79 See Chapter 7.3.1.(1)-(6) at pp. 285-291.

subsection (b) is to catch all other types of transactions constituting concentrations.⁸⁰ Hence, the particular merger definition of subsection (a) is rather technical and narrow⁸¹ Not surprisingly, thus, mergers in this technical sense are rare in practice,⁸² which is why the Commission only had to deal with very few of those cases.⁸³ However, this is basically a terminological question only as most transactions which would be called mergers in Britain and Germany are covered by the second type of concentration provided for in Article 3 (1) (b) of the Regulation, namely the acquisition of control, as the following paras will show.

(2) Acquisition of Control

This second type of concentration is of great practical relevance. The method through which control is acquired is irrelevant. Hence, unlike German law,⁸⁴ but in accordance with English law,⁸⁵ the Regulation does not attempt to describe the different types of transactions constituting concentrations exhaustively. Contrary to German law, there exist no specific thresholds indicating the acquisition of control.⁸⁶ Rather, methodically similar to English law,

80 In line with Art. 3 of the Third Council Directive (EEC) No. 78/855, [1978] O.J. L 295/36, concerning mergers of of public limited liability companies.

81 For a thorough analysis of the merger definition see *Cook/Kerse*, EEC Merger Control, Chapter 2.2.1. at p. 14-16.

82 *Bos/Stuyck/Wytinck*, Concentration Control in the EEC, para 4-027; *Downes/Ellison*, The legal control of mergers in the EC, p. 35; *Fine*, Mergers and Joint Ventures in Europe, para 4-006; *Drauz/Schröder*, Praxis der europäischen Fusionskontrolle, p. 186. According to *Löffler*, in *Langen/Bunte*, Kartellrecht, Art 3 FKVO 4064/89, Rn. 3 mergers within the meaning of Article 3(1)(a) account for less than 5 per cent of all concentrations vetted by the Commission.

83 *Renault/Volvo*, [1990] O.J. C 281/2 = CMLR 4 [1991] 297; *Kyowa/Saitama Banks*, [1991] O.J. C 66/13 = CMLR 4 [1991] 331; *Sanofi/Yves Saint Laurent*, [1993] O.J. C 89/3 = CMLR 4 [1993] 300; *AGF/La Unión y el Fénix*, [1994] C 155.

84 See Chapter 7.3.1. at pp. 283.

85 See Chapter 6.2.1. at pp. 214.

86 Sec. 23 (2) No. 2 GWB: 25 and 50 per cent. See Chapter 7.3.1.(2) at pp. 287.

control is defined in comprehensively broad terms. Yet, the notion of control differs from that of the Fair Trading Act. Whereas section 65 (3) of the British Fair Trading Act defines control as the ability “*directly or indirectly, to control or materially to influence the policy of a body corporate*”, Article 3 (3) of the Merger Regulation takes a significantly more restrictive approach defining control as the “*possibility of exercising decisive influence*.”

There already exists a considerable body of Commission case law interpreting what is meant by the “*possibility of exercising decisive influence*.”⁸⁷ Needless to say, the purchase of a majority stake providing *de jure* control confers *decisive influence*.⁸⁸ Matters become more difficult where minority stakes are concerned.⁸⁹ As a general rule, under the Merger Regulation, a minority holding is not considered to confer the *possibility of exercising decisive influence* and does therefore not constitute a concentration. There are, however, exceptions to this general rule.⁹⁰ A minority holding may confer *decisive influence* where the acquiror is granted far reaching rights giving him decisive influence in the articles of association or through binding shareholder agreements,⁹¹ or where he enjoys *de facto* control due to the remaining shares being widely dispersed. In *CCIE/GTE* (1992)⁹² the acquiror holding only a 19 per cent stake

87 For a complete list up to date to October 1995 of the numerous Commission decisions on the definition of concentration see *Jones/Van der Woude/Lewis*, E.C. Competition Law Handbook, 1996, pp. 707.

88 See for example *GEHE AG/OCP*, [1993] O.J. C 114/6: 50,1 %; *WestLB/Thomas Cook*, [1993] O.J. C 216/4: 86 %; *Sanofi/Yves Saint Laurent*, [1993] O.J. C 89/3: 51,6 %; *Dasa/Fokker*, [1993] O.J. C 136/4: 51 %; *Deutsche Bank/Banco de Madrid*, [1993] O.J. C 175/11: 100 %.

89 See also *Heidenhain*, in *EEC Merger Regulation*, Fordham 1993, pp. 452 who points out that the position on minority holdings, which were originally not thought to be covered by the Regulation, has changed since its introduction.

90 Decisive influence was held to exist in: *Banesto/Totta*, [1992] O.J. C 107/25: 46,5 %; *Arjomari/Wiggins Teape Appleton*, [1990] O.J. C 321/16: 39 %; *Société Générale de Belgique/Générale de Banque*, [1993] O.J. C 225/2: 26,96 %. No decisive influence was found in *Mediobanca/Generali*, [1991] O.J. C 334/23: 12,8 %.

91 See *CCIE/GTE*, [1992] O.J. C 258/15; *Conagra/Idea*, [1991] O.J. C 175/18. The latter case is discussed below in connection with the acquisition of joint control, Chapter 8.3.1(3) at pp. 375.

92 *CCIE/GTE*, [1992] O.J. C 258/15.

was considered to have decisive influence as he enjoyed extensive contractual rights, inter alia, to determine the business policy of the controlled undertaking and to veto all decisions of strategic importance. In *Arjomari/Wiggins Teape Appleton* (1990)⁹³ Arjomari acquired a 39 per cent stake in Wiggins which was held to confer *de facto* control on the ground that the remaining shares were widely dispersed among 107.000 shareholders none of whom held a stake exceeding 4 per cent. More recently, in *Société Générale de Belgique/Générale de Banque* (1993)⁹⁴ where *Société Générale* increased its holding in *Générale de Banque* from 20,94 to 25,96 per cent the Commission decided that a concentration had occurred as the previous 20,94 per cent stake conferred, due to the relatively low level of participation in the general meetings, a *de facto* voting power of about 45 per cent in the annual general meeting whereas the increased holding of 25,96 per cent would give *Société Générale* a *de facto* voting power in the annual general meeting of about 56 per cent. In *Ford/Hertz* (1994), however, the Commission held that the increase from a 49 per cent stake to a 54 per cent holding may not be considered a concentration as the *quality* of the *decisive influence* already exercised before the acquisition did not intensify.⁹⁵ The passage from joint control to sole control is, however, considered a concentration as the Commission pointed out in *ICI/Tioxide* (1990).⁹⁶

Concerning the issue of minority stakes, the Merger Regulation is more lenient than both British and German law in the sense that in the latter jurisdictions the acquisition of a substantial minority holding regularly constitutes a merger whereas it may only in exceptional cases be considered a concentration under the Regulation. This is most manifest in comparison to German law where section 23 (2) No. 2 GWB stipulates that in any case the acquisition of a 25 per

93 *Arjomari/Wiggins Teape Appleton*, [1990] O.J. C 321/16.

94 *Société Générale de Belgique/Générale de Banque*, [1993] O.J. C 225/2.

95 *Ford/Hertz*, [1994] O.J. C 121/4.

96 *ICI/Tioxide*, [1990] O.J. C 304/27.

cent-stake is to be considered a merger, and, moreover, section 23 (2) No. 6 GWB allows for even smaller stakes to be considered a merger if those stakes confer “*directly or indirectly an influence which is material with respect to competition.*”⁹⁷ British law is at least in its practical effect largely in harmony with German law in this respect for section 65 (3) of the Fair Trading Act defines control, albeit in its mildest form, as the ability “*materially to influence the policy of a body corporate*” which is clearly less than “*decisive influence*”. Although no fixed thresholds are applied in Britain, as in Germany a 25 per cent stake is almost certain to fall under the merger definition of the Fair Trading Act, and the OFT has indicated that holdings in excess of 15 per cent are liable to be examined in order to assess whether they confer the ability “*materially to influence the policy*” of another company.⁹⁸ Hence, both British and German merger control law covers transactions which would (at present) not be considered a concentration under the European Merger Regulation. Hence, due to the comparatively narrow definition of concentrations under the Merger Regulation, its applicability in terms of transactions covered is somewhat restricted. However, as the definition of concentrations through acquisitions under the Regulation (*the possibility of exercising decisive influence*) is open to interpretation, it appears, in particular in the light of the history of European merger control law, that there is a risk or a chance - depending one’s viewpoint - that in the long run the interpretation of this definition is broadened by the European Commission, the European Court of Justice, and the European Court of First Instance through case law in order to expand the European jurisdiction through the back-door.

A noteworthy practical consequence of the divergencies in the respective merger or concentration definitions under European,

97 For details see Chapter 7.3.1. at pp. 283. As to these aspects see also *Bechtold*, Antitrust law in the European Community and Germany - An uncoordinated co-existence?, Fordham 1992, pp. 343, 352, 355.

98 For details see Chapter 6.2.1. at pp. 214.

British, and German law is that the British and German merger control rules may apply to transactions having a *Community dimension* as defined by Article 1 (thresholds), but which are nevertheless not caught by the European Merger Regulation because of its narrower definition of a concentration with respect to minority stakes. This result appears somewhat inconsistent with the philosophy of the Merger Regulation as certain mergers despite having a *community dimension* are now as before assessed by - one or more - national authorities. In order to avoid these inconsistencies, a uniform merger or concentration definition in both the European Merger Regulation and the national merger control laws of the Member States appears desirable.

(3) Joint Control - Joint Ventures

Under the Merger Regulation, not only the acquisition of sole, but also of joint control constitutes a merger. This latter form of concentration accounts for almost half of all concentrations notified as Table 20 above at page 343 demonstrates. Hence, the acquisition of joint control is of major practical relevance.⁹⁹

The classic case of joint control is where two parent companies hold a 50 per cent stake each in a subsidiary.¹⁰⁰ In this sort of deadlock-situation decisions may only be taken jointly. The same holds true if two or more parent companies hold stakes below 50 per cent as long as the important strategic decisions in the jointly owned company have to be taken jointly by the parents (deadlock-

99 As to the relevance joint acquisitions in practice see *Löffler*, in *Langen/Bunte, Kartellrecht*, Art. 3 FKVO 4064/89, Rn. 24.

100 *Volvo/Atlas*, [1992] O.J. C 17/10; *Mondi/Frantschach*, [1992] O.J. C 124/23; *Pechiney/Viag*, [1993] O.J. C 307/7; *Höchst/Wacker*, [1993] O.J. C 171/4; *BHF/CCF/Charterhouse*, [1993] O.J. C 247/4.

situation).¹⁰¹ An example is *Conagra/Idea* (1991) where the U.S. corporation *Conagra* acquired a 26 per cent stake¹⁰² in the French company *Idea*.¹⁰³ In addition to the 26 per cent voting rights, *Conagra* entered into a shareholders' agreement with the other remaining *Idea*-shareholder, who held 74 per cent of the voting rights. According to this shareholders' agreement *Conagra* secured for itself a number important veto rights and was therefore considered to have joint "*decisive influence*" over *Idea*. Among these veto rights were, inter alia, the approval of the annual budget; approval of investments exceeding 1.5 million French francs; approval of the development of new products costing more than 1.5 million French francs; and the approval of the employment and salary of senior executives. Hence, in cases where two or more companies hold stakes in a joint venture differing in size and voting power, it depends very much on the circumstances of the individual case (shareholders' agreements, articles of association) whether these companies can be considered to have joint control.¹⁰⁴

However, a joint venture jointly controlled by its parent companies is to be considered a concentration within the meaning of Article 3 (1) of the Regulation only if it is of a *concentrative* rather than a *co-operative* nature.¹⁰⁵ According to Article 3 (2) of the

101 Renault/Volvo, [1990] O.J. C 281/2: 45:45 %; Elf/BC/CEP-SA, [1991] O.J. C 172/8: 34:34 %; Fortis/CGER, [1994] O.J. C 23/13: 49,9:49,9 %; Sextant/BGT-VDO, [1993] O.J. C 9/3: 50,5:49,5 %; Continental/Kaliko/DG-Bank/Benecke, [1993] O.J. C 336/11: 50,1:49,9 %; Conagra/Idea, [1991] O.J. C 175/18: 20:74 %.

102 The stake in terms of capital amounted to only 20 per cent.

103 Conagra/Idea, [1991] O.J. C 175/18. For a discussion of this case see Jones/González-Díaz, The EEC Merger Regulation, p. 6; Löffler, in Langen/Bunte, Kartellrecht, Art. 3 FKVO 4064/89, Rn. 12.

104 For further details are provided in the Commission notice on the notion of a concentration under Council Regulation (EEC) No. 4064/89: see [1994] O.J. C 385/5. Reproduced in Jones/Van der Woude/Lewis, E.C. Competition Law Handbook, 1996, pp. 670, para 2.

105 See the Commission Notice on the distinction between concentrative and co-operative joint ventures und Council Regulation 4064/89, [1994] O.J. C 385/1. There exists a vast amount of publications on the controversial demarcation between concentrative and co-operative joint ventures. For a very clear and precise analysis see Jones/González-Díaz, The EEC Merger Regulation, p. 51-78. Also Brown, Distinguishing between Concentrative and Co-operative Joint Ventures: Is it Getting any Easier?,

Regulation a joint venture is to be considered concentrative if it performs “*on a lasting basis all the functions of an autonomous economic unity, which does not give rise to coordination of the competitive behaviour of the parties amongst themselves or between them and the joint venture.*” A crucial factor is the complete and permanent absence of the parent companies from the joint venture’s market. Joint ventures not meeting the criteria outlined above are excluded from the scope of the Regulation. They are assessed under the much stricter regime of Articles 85 and 86 of the EC-Treaty. The underlying rationale behind this drastic differentiation between concentrative and co-operative joint ventures is that only concentrative joint ventures amount to “real” mergers in terms of structural market change whereas co-operative joint ventures tend to be “*back-door cartels*” rather than concentrations. As cartels are generally considered more harmful to competition than mergers, since mergers might have numerous beneficial effects, most jurisdictions, including Britain and Germany, treat mergers much more favourably than cartels. The same holds true on European level which is why the differentiation between concentrative (Merger Regulation) and co-operative joint ventures - meaning disguised cartels - (Articles 85 and 86 of the EC-Treaty) is so important in practice.¹⁰⁶

8.3.2. Community Dimension

According to Article 1 (2) of the Regulation, “*a concentration has*

[1996] 4 ECLR 240-249; *Burnside/Mackenzie*, Joint Venture Analysis: The latest chapter, [1995] 3 ECLR 138-146; *Hawk/Huser*, A *Bright* line shareholding test to end the nightmare under the EEC Merger Regulation, [1993] CMLREV 1155-1183.

106 As to the scope for reform of this differentiation see *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, paras 98-121.

a Community dimension where:

- (a) *the combined aggregate worldwide turnover of all the undertakings concerned is more than ECU 5.000 million; and*
- (b) *the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than ECU 250 million,*

unless each of the undertakings concerned achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State."

This three-part *Community-dimension* test is based on turnover figures,¹⁰⁷ which is in principle in line with the quantitative jurisdictional test applied in Germany. However, unlike the quantitative tests applied in Britain¹⁰⁸ (asset test or market share test) and Germany¹⁰⁹ (turnover thresholds), the *Community-dimension* test also defines the scope of the extraterritorial applicability of the Regulation as the following analysis of the three elements of the *Community-dimension* test will show.

107 Concerning the calculation of turnover, the Regulations contains detailed rules in Art. 5 which will not be discussed in this work. Turnover is defined by Art. 5 (1) as follows: "*Aggregate turnover within the meaning of Article 1 (2) shall comprise the amounts derived by the undertakings concerned in the preceding financial year from the sale of products and the provision of services falling within the undertakings' ordinary activities after deduction of sales rebates and of value added tax and other taxes directly related to turnover.*" For a detailed examination of the calculation rules see *Jones/González-Díaz*, *The EEC Merger Regulation*, p. 16-30; *Fine*, *Mergers and Joint Ventures in Europe*, paras 4-070 to 4-095; *Drauz/Schröder*, *Praxis der europäischen Fusionskontrolle*, p. 16-30; *Löffler*, in *Langen/Bunte*, *Kartellrecht*, Art 5 FKVO 4064/89, Rn. 1-17.

108 See Chapter 6.2.2. at pp. 217. The assets test is satisfied where the gross value of the world-wide assets taken over exceed £70 million. The market share test is satisfied if the merger results in a market share of at least 25 per cent.

109 See Chapter 7.3.2. at pp. 293. The basic rule is that mergers are exempted from control where the joint turnover proceeds of the participating enterprises amounted to less than DM 500 million in the preceding business year.

(1) World-wide turnover of ECU 5.000 million

The combined aggregate world-wide turnover of the participating enterprises has to exceed ECU 5.000 million. As *Christopher Jones* of the DG IV put it, this basic quantitative test rests upon the “*partial fiction*” that mergers between very large companies or groups with significant financial power are more likely to have Community-wide effects than smaller ones.¹¹⁰ Legally, the turnover-criterion is not an ideal criterion or, again in the words of *Christopher Jones*, a “*rather crude test*” since mergers in specific specialist markets, which are not turnover-intensive, but equally important to the common market as a whole, may as well seriously affect the competitive conditions.¹¹¹ However, the turnover of a company or group is relatively easy to ascertain and the turnover criterion therefore easy to handle for both the enterprises involved and the Commission.

Another question is,¹¹² however, whether the current turnover-threshold of ECU 5.000 million, which amounts to more than £4.000 million, is a realistic one.¹¹³ According to the 1996 Commission Green Paper on Merger Control, out of the largest 2.200 European companies only 152 companies in the EC and EFTA States had in 1993 a world-wide turnover exceeding ECU 5.000 million.¹¹⁴ This gives an idea of how large the participating enterprises have to be in order to come within the reach of the Merger Regulation. Obviously, the very high level of the turnover threshold is the result of a political compromise designed not to hand over too much power to the

110 *Jones/González-Díaz*, The EEC Merger Regulation, p. 15, 19.

111 *Jones/González-Díaz*, The EEC Merger Regulation, p. 38. See also the analysis by the *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, paras 31 et seq.

112 As to the current debate on the threshold issue see Chapter 8.3.2.(4) at pp. 367.

113 Currency rate as of June 14, 1996 (*Financial Times*) £1 = ECU 1,248.

114 *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, para 46.

Commission.¹¹⁵

(2) Community-wide turnover of ECU 250 million

According to Article 1 (2) (b) of the Regulation, concentrations meeting the ECU 5.000 million world-wide threshold test come under the jurisdiction of the Commission only if at least two of the participating enterprises have a turnover of ECU 250 million or more Community-wide. This element has a double function.

First, it is an additional quantitative criterion excluding smaller concentrations by focusing on the turnover within the common market (*de minimis* rule).¹¹⁶

Secondly, the ECU 250 million Community-wide turnover requirement has the important legal function of determining the extra-territorial jurisdiction of the Commission concerning companies not resident in EC Member States:¹¹⁷ as long as the Community-wide thresholds are achieved it does not matter where the merging enterprises are incorporated. An example is *Kyowa/Saitama Banks (1991)*¹¹⁸ where two large Japanese banks merged which had branches in Europe meeting the ECU 250 million turnover threshold. As the merger did not raise any competition concerns within Europe it was cleared swiftly. A parallel situation arose in *Bank America/Security Pacific (1991)*¹¹⁹ where the merging U.S. banks

115 See *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, para 46. Also *Bright*, The European Merger Control Regulation: Do Member States still have an independent role in merger control? [1991] 4 ECLR 139.

116 See *Jones/González-Díaz*, The EEC Merger Regulation, p. 15; *Löffler*, in *Langen/Bunte*, Kartellrecht, Art 1 FKVO 4064/89, Rn. 21.

117 *Jones/González-Díaz*, The EEC Merger Regulation, pp. 88; *Löffler*, in *Langen/Bunte*, Kartellrecht, Art 1 FKVO 4064/89, Rn. 26.

118 *Kyowa/Saitama Banks* [1991] O.J. C 66/13.

119 *Bank America/Security Pacific*, [1991] O.J. C 289/14.

met the turnover thresholds in Europe. Again, in the absence of any anti-competitive effects on the European market the merger was waved through quickly. Apparently, the application of the Merger Regulation to non-European mergers has as yet not led to any legal or political problems comparable to those experienced in Germany where the FCO prohibited a number of “*foreign*” mergers.¹²⁰

Being based on the turnover achieved in Europe, the Merger Regulation defines its jurisdictional reach different from both British and German law. In order to be applicable, the Fair Trading Act requires that of the merging enterprises “*one at least was carried on in the United Kingdom or by or under the control of a body corporate incorporated in the United Kingdom*”¹²¹ while the German GWB declares itself applicable to all restraints of competition which have “*effects*” within Germany.¹²² Compared to the British and German law, the turnover-based criterion applied by the Merger Regulation is much easier to handle as the turnover achieved in Europe is a criterion simple to ascertain. However, it is also far less flexible than the more vague but considerably broader concepts of ‘*business carried on Britain*’ or ‘*anti-competitive effects within Germany*.’ Although the test applied by the Merger Regulation provides for a maximum of legal certainty and practicability, it appears full of gaps as concentrations between companies where at least one does not reach the ECU 250 million threshold may very well have serious anti-competitive effects on the common market which can not be remedied properly by a national merger control authority. For example, if a powerful European company meeting all turnover thresholds merged with an equally strong U.S. company not active on the European market, the merger might still affect competition in the common market: global competition might be significantly reduced as a result of the transaction which would in turn in the long

120 See Chapter 7.3.3. at pp. 295.

121 Sec. 64 (1) FTA 1973. See Chapter 6.2.4. at pp. 219.

122 Sec. 98 (2) GWB. See Chapter 7.3.3. at pp. 295.

run enable the European player to raise prices within the common market above the competitive level without having to fear new market entry (oligopoly situation). Yet, the Merger Regulation would not be applicable.

(3) Two-thirds Rule

Despite achieving a joint aggregate world-wide turnover of more than ECU 5.000 million and a Community-wide turnover of ECU 250 million each, a concentration does not fall under the jurisdiction of the Commission if each of the participating enterprises achieves more than two-thirds of its aggregate Community-turnover in one and the same Member State.¹²³ This last element of the Community-dimension-test is designed to exclude from the Commission's jurisdiction concentrations which predominantly affect only one Member State.¹²⁴

(4) New Developments

As the definition of *Community dimension* is the decisive factor in the division of jurisdiction between the Commission and the

123 The wording is interpreted restrictively by the Commission in the sense that the two-thirds turnover must be achieved by each enterprise in the same Member State, say Britain. The rule does not apply to a situation where each participating company achieves two-thirds of its turnover in its respective home country, for example British company A in the U.K., German company B in Germany, and French company C in France. See *Mitsubishi/Ucar*, [1991] O.J. C 5/7; *Digital/Kienzle*, [1991] O.J. C 56/16; *Cargill/Unilever*, [1990] O.J. C 327/14.

124 Although there have been occasional calls for a deletion of the two-thirds rule or for its replacement by a three-quarters rule, the Commission considers the two-thirds balance best suited to keep predominantly national mergers out of its scope. As to further references see *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, paras 60 and 66.

Member States and, moreover, since the thresholds introduced in 1990 were very much the result of a political compromise,¹²⁵ Article 1 (3) of the Regulation requires a review of these thresholds before the end of the fourth year following the adoption of the Regulation. Pursuant to this provision, the Commission has examined the adequacy of the thresholds in 1993¹²⁶ and again in 1996¹²⁷ and concluded both times - as one would expect - that there are strong arguments in favour of a reduction of the current thresholds. Put simply, in order to come closer to achieving a level playing field and to avoid the problems connected with multiple national filings, in particular the risk of conflicting decisions by different national merger control authorities, the Commission proposes a reduction of the current thresholds to ECU 2.000 million world-wide and ECU 100 million Community-wide, but to maintain the two-thirds rule unchanged. The Commission estimates that this would increase its workload by an extra 65 to 80 cases per annum.¹²⁸

Legally and from a European point of view, the Commission's arguments are compelling. However, the current debate is less legal than political. As the reduction of thresholds as proposed by the Commission would extend its jurisdiction considerably and at the same time restrict the Member States' powers to vet large cross-border mergers, it is not surprising that the proposed changes have - according to press reports - been rejected by a number of Member States including Britain and Germany.¹²⁹

In Britain any further increase of the Commission's power seems

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- 125 *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, para 32; *Löffler*, in *Langen/Bunte*, *Kartellrecht*, Art 1 FKVO, Rn. 7
- 126 Commission Report to the European Council on the review of the Merger Regulation, COM (93) 385 final of 28 July 1993.
- 127 *EC-Commission*, Green Paper on the Review of the Merger Regulation, COM (96) 19 final.
- 128 *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, para 69.
- 129 *Frankfurter Allgemeine Zeitung*, February 1, 1996; *Financial Times*, November 15, 1996.

to have been rebuffed categorically as a matter of principle. The German government has also given a mixed reaction as it appears to fear that a more powerful Commission would lead to a shift from competition policy to industrial policy which is opposed in Bonn and Berlin. Instead, the Germans are opting for an independent European competition authority as discussed above.¹³⁰ The French apparently consider a reduction of the thresholds not necessary due to the effect of inflation and the enlargement of the European Union which makes it easier for companies to achieve the Community-wide turnover thresholds. Although the French undoubtedly have a point, given the very high level of the present thresholds it appears arguable whether really all concentrations having a Community-dimension in a material sense are covered by the Regulation. Yet, due to inflation time clearly is on the Commission's side.

Probably foreseeing the political opposition to its reduction plans, the Commission offers a second-best, more limited solution in order to address at least the problem of multiple filings: where concentrations below the *Community-dimension* thresholds come within the jurisdiction of more than one national merger control system, the Commission's competences could be extended automatically to cover those mergers or, alternatively, the participating companies could be given a right to choose between either multiple national or single-stop Community merger control.¹³¹

From a strictly legal and pragmatic point of view, the reduction of thresholds seems preferable as it guarantees a higher degree of legal certainty. Only in case of a threshold reduction - as opposed to the multiple-filing test - does the jurisdiction of the Commission not depend on national merger control law. Moreover, the question whether a particular transaction would be subject to multiple national filings can be difficult to ascertain for the Commission and is in any

130 Chapter 8.2.1. at pp. 344.

131 *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, paras 84 et seq.

case time-consuming for the companies involved. However, as a threshold reduction appears unlikely at present for political reasons, if there is to come any change in the near future (which the author doubts), it is probably going in the direction of the second best multiple-filing solution.

8.3.3. Referrals to and from Member States

Pursuant to the one-stop shop principle, the allocation of jurisdiction as outlined in Article 1 rests upon the basic rule that concentrations having a *Community-dimension* are assessed exclusively by the Commission while those below the *Community-dimension* thresholds fall under the jurisdiction of the competent national authorities. As practicable and clear as the *Community-dimension* test based on turnover-thresholds might be, it is undisputedly a rather crude test since high turnover proceeds of the merging enterprises are as such no indicator of the likely (anti-) competitive effects a concentration might have. Hence, there is a regulatory need to refine the basic unsubtle threshold test of Article 1 which is the function of Article 9, Article 22 (3), and Article 21 (3) of the Merger Regulation.

(1) German Clause: Referral to Member States

According to Article 9, a Member State may request the referral of a concentration to its own merger control authorities if that concentration

“threatens to create or to strengthen a dominant position as a result of which effective competition would be significantly

impeded on a market, within that Member State, which presents all the characteristics of a distinct market, be it a substantial part of the common market or not."

Hence, Article 9 is an exception to the rule that concentrations with a *Community-dimension* are vetted exclusively by the Commission. Broadly speaking, Article 9 is based on the thought that concentrations with a predominantly national impact are better controlled at national level and is therefore very much in line with the principle of subsidiarity contained in the EC-Treaty.¹³² Surprisingly, this rather sensible provision was introduced virtually at the last minute on the initiative of the German delegation backed by the British, which is why this rule is generally called "*German Clause*".¹³³

If the substantive conditions of Article 9 are met, namely the threat of a dominant position confined to a distinct national market, the Commission has discretion to either deal with the case itself or refer it to the competent national merger control authorities.

Thus far, the provision has played a rather limited role only, which could of course change rapidly if the Community-dimension thresholds were to be reduced.¹³⁴ Albeit the Commission has received a total of 10 referral requests - eight from Germany (!), one from Britain, and one from France,¹³⁵ only three referrals - one to each of the requesting Member States - were granted by the Commission.¹³⁶ Hence, it appears that the Commission interprets Article 9 restrictively and does in no way follow the Member States'

132 Article 3b of the EC-Treaty.

133 As to the history of Art. 9 see *Löffler*, in *Langen/Bunte*, *Kartellrecht*, Art 9 FKVO, Rn. 2.

134 *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, para 93.

135 As of 31 December 1995. Information provided by *Löffler*, in *Statistik der EG-Fusionskontrollverfahren nach fünfjähriger Anwendungspraxis*, *WuW* 1996, 209, 211.

136 Britain: *Tarmac/Steetly*, [1992] O.J. C 50/25 = CMLR 4 [1992] 343; Germany: *McCormick/CPC/Radoank/Ostmann*, *WuW/E* EV 2157; France: *Holdercim/Cedest*, [1994] C 211/4.

requests blindly. For example, in *Alcatel/AEG Kabel (1991)*¹³⁷ which concerned a concentration in the telecommunication and power cables market, the Commission disagreed openly with the FCO's contention in the referral request that there was a distinct German market for telecommunication cables and that, although there was undisputedly a distinct market for power cables, the proposed concentration would threaten to create or strengthen a dominant position. If a case is referred to a Member State, this state applies its national merger control law, but is restricted in that it "*may only take the measures strictly necessary to safeguard or restore effective competition on the market concerned.*"¹³⁸

The British case referred back, *Tarmac/Steetly (1992)*,¹³⁹ illustrates well the kind of situation Article 9 was designed to cover: *Tarmac Plc* and *Steetly Plc*, both U.K. companies active in various building products sectors, created a concentrative joint venture to which they ceded, inter alia, all their U.K. assets, employees and business relating to the manufacture and sale of building bricks and clay roofing tiles. The concentration easily passed the *Community-dimension* test. On request by the British government, however, the Commission found that, basically due to high transport costs, there existed distinct markets within which the concentration threatened to create a dominant position. Concerning bricks the North-East and South-West of England and for tiles Great Britain as a whole were considered distinct markets within the meaning of Article 9. Since the concentration evidently had no material cross-border impact, there was no need for the Commission to be involved. Following the

137 *Alcatel/AEG Kabel*, [1992] O.J. C 6/23 = CMLR 4 [1992] 80 = WuW/E EV 1713, 1714. Following this decision the FCO intended to challenge the Commission's decision before the ECJ, but this was not considered politically opportune by the German government, see *Löffler*, in *Langen/Bunte*, Kartellrecht, Art 5 FKVO, Rn. 5.

138 Art. 9 (8) of the Regulation.

139 *Tarmac/Steetly*, [1992] O.J. C 50/25 = CMLR 4 [1992] 343 = WuW/E EV 1814. For a more detailed discussion of this case see *Jones/González-Díaz*, The EEC Merger Regulation, p. 42.

referral, the parties gave up their merger plans.

The German case referred back, *McCormick/CPC/Rabobank/Ostmann* (1993),¹⁴⁰ cannot be considered a “typical” Article 9 case as it was not referred voluntarily. The case concerned the creation of a concentrative joint venture which was to combine the entirety of *McCormick*’s (U.S.) and *CPC*’s (U.S.) herb and spice business in the EC and EFTA countries with the assets of *Ostmann*, the leading German company in that market. The concentration would mainly have affected the German market for dried herbs and spices. That market was considered a distinct market within the meaning of Article 9 by the German government as in Germany suppliers were basically German companies. Although the Commission agreed with this opinion, it had intended to deal with the concentration itself as it had international implications. However, this option had been foreclosed as a result of an error in the calculation of the legal deadlines provided for in Article 10 (1). Pursuant to Article 10 (6) the only option left open was to refer the case to the FCO. Following the referral, the parties withdrew their proposed concentration.

(2) Dutch Clause: Referral to the Commission

Acknowledging the fact that many concentrations that do not have a *Community-dimension* as defined by Article 1 do in reality have significant European cross-border effects, Article 22 (3) of the Regulation stipulates that at the request of a Member State a concentration creating or strengthening a dominant position in the requesting Member State but *not* having a *Community-dimension* may be referred to the Commission provided the concentration affects trade between Member States. Thus, Article 22 (3) is an

140 *McCormick/CPC/Radoank/Ostmann*, WuW/E EV 2157.

exception to the rule that those concentrations not meeting the *Community-dimension* thresholds fall under the jurisdiction of the Member States and has, thus, the opposite function of Article 9. Parallel to Article 9, however, is the restriction of power: In remedying the anti-competitive effects the Commission is confined to those measures strictly necessary to maintain or restore effective competition within the territory of the Member State at the request of which it intervenes.¹⁴¹

As with Article 9, Article 22 (3) was also inserted virtually at the last minute, this time, however, at the behest of those smaller Member States which have, or had at that time, no merger control law, most notably the Netherlands (therefore Dutch Clause).¹⁴²

Not surprisingly therefore, the two requests which have been lodged under Article 22 (3) so far¹⁴³ came from smaller Member States, namely Belgium and the Netherlands. The first case, *British Airways/Dan Air* (1993),¹⁴⁴ was declared compatible with the common market during phase 1 of the Commission's investigations while the second referred concentration, *RTL/Veronica/Endemol* (1995),¹⁴⁵ was prohibited.

Although in the two cases mentioned above no jurisdictional problems arose, dogmatically Article 22 (3) appears not to have been thought through thoroughly as it may lead to conflicting decisions which is just what the Regulation aims to avoid.¹⁴⁶ If a cross-border concentration not meeting the *Community-dimension* thresholds is notified to multiple national merger control authorities and one of these authorities makes an Article 22 request, conflicting decisions of the Commission and the remaining national authorities investigating

141 Art. 22 (5) of the Regulation.

142 *Löffler*, in Langen/Bunte, Kartellrecht, Art 22 FKVO, Rn. 3.

143 As of end of 1995.

144 *British Airways/Dan Air*, [1993] O.J. C 68/5 = CMLR 4 [1993] 235 = WuW 1993, 286.

145 *RTL/Veronica/Endemol*, [1996] O.J. L 134/33.

146 *Jones/González-Díaz*, The EEC Merger Regulation, p. 47.

the concentration might result. Take, for example, the *British Airways/Dan Air* (1993) case.¹⁴⁷ In this case concerning the air transport market, in particular the route Brussels-London, the U.K. authorities cleared the merger, while Belgium lodged an Article 22 (3) request to get the concentration vetted by the Commission. As the Commission cleared the deal, no problem arose. But what if the Commission had blocked the concentration? What if London had blocked the merger while Brussels cleared it?

Yet, these inconsistencies should not be overestimated. As more and more Member States have introduced national merger control laws, Article 22 (3) cannot be expected to be invoked very often in future,¹⁴⁸ which is particularly true if the Community-dimension thresholds are reduced or the “multiple filing solution”¹⁴⁹ is introduced as in this case most significant cross-border concentrations would fall under the scope of the Merger Regulation anyway.

(3) “Legitimate Interests” of Member States

Article 21 (3) provides that “*Member States may take appropriate measures to protect legitimate interests other than those taken into consideration by this Regulation and compatible with the general principles and other provisions of Community law.*” The provision specifies as examples for legitimate interests public security, plurality of the media, and prudential rules. Before any “*appropriate measures*” may be taken by a Member State the legitimate interest

147 *British Airways/Dan Air*, [1993] O.J. C 68/5 = CMLR 4 [1993] 235 = WuW 1993, 286.

148 The Commission intends to keep Art. 22 (3) as a “useful tool, especially for those Member States that do not currently have a merger control system.” See *EC-Commission*, Green Paper on the Review of the Merger Regulation, 1996, para 97.

149 See Chapter 8.3.2.(4) at pp. 367.

claimed must be formally recognized by the Commission.¹⁵⁰

The Member States' right to invoke legitimate interests is, however, restricted in a number of ways. Legitimate interests may not include competition considerations as these are reserved for the Commission (one-stop shop principle). Hence, there is no risk of conflicting decisions. It follows that a Member State may not allow a concentration on legitimate interest grounds which was previously blocked by the Commission on competition grounds. A concentration blocked by the Commission remains blocked. Consequently, the legitimate interests provision is of relevance only in cases where the Commission has already cleared the concentration and the Member State wants to block it. Lastly, the Regulation does not create any new rights for the Member States to prohibit concentrations. Article 21 (3) simply refers to those legitimate interest provisions already contained in the national law, as for example, section 84 (1) of the British Fair Trading Act 1973 (public interest).

Since the entry into force of the Regulation until the end of 1995, Article 21 (3) has only once been resorted to. This case concerned a bid by *Lyonnaise de Eaux SA* of France for *Northumbrian Water Group Plc* of the U.K in 1995.¹⁵¹ The Commission recognized that under the regulatory system of the British *Water Industry Act 1991*¹⁵² the Director General of the Water Service (DGWS) has to have, as a substitute for real competition which is not possible in this sector, the ability to make comparisons between different water companies. This ability would have been prejudiced by the loss of *Northumbrian Water* as an independent water company. The Commission held that the DGWS' ability to make comparisons constituted a legitimate interest within the meaning of Article 21 (3) of

150 Commission decision of 29.3.1994, Water Industry Act, WuW 1995, 945, 946.

151 As to the *MMC* report on the proposed merger: *Lyonnaise des Eaux SA* and *Northumbrian Water*, July 1995, Cm 2936. The *MMC* recommended that the bid could go ahead if substantial cuts in charges to customers were agreed in advance with the water regulator.

152 In particular sec. 32-34 of the Water Industry Act 1991.

the Regulation.¹⁵³ However, the Commission prohibited the U.K. merger control authorities from taking into account the potential implications of the merger for competition, employment and regional policy¹⁵⁴ as these are consideration reserved for the Commission.

8.4. The Substantive Appraisal Criteria

Article 2 (3) of the Merger Regulation stipulates that “a *concentration which creates or strengthens a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part of it shall be declared incompatible with the common market.*”¹⁵⁵

On the face of it, it appears that the Regulation requires a two-part test¹⁵⁶ consisting of

- (1) *the creation or strengthening of a dominant position, and*
- (2) *a significant impediment of effective competition.*

In practice, however, the Commission has never explicitly applied the second part of the test.¹⁵⁷ Rather, as one would expect, the Commission continued to apply the definition of a dominant position already used under Article 86 of the EC-Treaty, which prohibits the *abuse* of a dominant position.¹⁵⁸ Now as before, a

153 Commission decision of 29.3.1994, Water Industry Act, WuW 1995, 945.

154 This was at least the interpretation which the Commission's decision was given by the *MMC*, see *MMC*, *Lyonnaise des Eaux SA and Northumbrian Water*, July 1995, Cm 2936, para 1.9.

155 The following paras are concerned with single market domination. As to oligopolistic market power see *Briones*, *Oligopolistic Dominance: Is there a Common Approach in Different Jurisdictions? A Review of Decisions Adopted by the Commission under the Merger Regulation*, [1995] 6 ECLR 334-347.

156 *Brittan*, *The Law and Policy of Merger Control in the EEC*, (1990) 15 ELR 351, 352.

157 *Fine*, *Mergers and Joint Ventures in Europe*, paras 4-155 et seq.

158 *Downes/MacDougall*, *Significantly Impeding Effective Competition: Substantive Appraisal under the Merger Regulation*, (1994) 19 ELR 286,

dominant position is defined as a position “*of economic strength enjoyed by an undertaking which enables it to hinder the maintenance of effective competition on the relevant market by allowing it to behave to an appreciable extent independently of its competitors and customers and ultimately of consumers.*”¹⁵⁹

Subsection (b) of Article 2 (1) lists a number of criteria which are of relevance in assessing whether a dominant position is to be expected as a result of the concentration, namely

- (a) *the market position of the undertakings concerned*
- (b) *their economic and financial power*
- (c) *the alternatives available to suppliers and users*
- (d) *their access to supplies or markets*
- (e) *any legal or other barriers to entry*
- (f) *supply and demand trends*
- (g) *the interests of the intermediate and ultimate consumers*
- (h) *the development of technical and economic progress provided that it is to consumers’ advantage and does not form an obstacle to competition.*

Apart from the last criterion, the criteria enumerated above are clearly competition related. A “balancing clause” as known in German law does not exist.¹⁶⁰ The test of market dominance, however, is basically in line with German law as defined in Section 24 (1) of the GWB.¹⁶¹ Under both legal frameworks the notion of dominance is based on the concept of the merged

293; Jones/González-Díaz, The EEC Merger Regulation, p. 130; Löffler, in Langen/Bunte, Kartellrecht, Art 2 FKVO, Rn. 41.

159 NV Nederlandsche Banden-Industrie Michelin v. Commission, [1985] 1 CMLR 282. For a similar definition under the Merger Regulation see e.g. *Tetra Pak/Alfa-Laval*, [1991] O.J. L 290/35 para 3.4: “*In the light of the above, the Commission considers that the unlikely occurrence of entry on the market means that in this respect Tetra Pak will not be constrained from acting to an appreciable extent independently of its competitors, customers, and ultimately consumers.*”; *Aerospatiale-Alenia/de Haviland*, [1991] O.J. L 334/42, para 72.

160 Chapter 7.5.3. at pp. 330.

161 See Chapter 7.5. at pp. 315.

enterprises being able to act independently of competitors and customers. British merger control law, in contrast, is based on the public interest criterion and differs therefore from the outset, although competition is by far the single most important public interest factor considered by the U.K. merger control authorities as has been demonstrated in Chapter 6.4.¹⁶² The following paragraphs examine the substantive criteria applied by the Commission in more detail. However, it should be borne in mind that although the Regulation has been in force for more than five years the case material available is still very limited since there have been only four prohibitions¹⁶³ and only 19 in-depth Phase 2 investigations until the end of 1995.

8.4.1. Market Share

As in Britain and Germany, the first step in the competition assessment after defining the relevant product and geographic market¹⁶⁴ is to look at the market shares the merging enterprises would achieve. Unlike Germany, where a 33 per cent market share leads to a legal presumption of market domination,¹⁶⁵ no presumptions as to a dominant position are contained in the European Merger Regulation. Rather on the contrary: Recital 14 of the Preamble of the Regulation stipulates that a concentration may be “*presumed to be compatible with the common market*” if “*the market share of the undertakings concerned does not exceed 25 per*

162 See pp. 245.

163 Aérospatiale-Alenia/de Havilland (2.10.91), [1991] O.J. L 334/42 = CMLR 4 [1991] M2; MSG Media Service (9.11.94), [1994] O.J. L 364/1; Nordic Satellite Distribution, [1996] O.J. L 53/10; RTL/Veronica/Endemol, [1996] O.J. L 134/33.

164 As to these aspects see in detail *Fine*, Mergers and Joint Ventures in Europe, p. 183-202; *Jones/González-Díaz*, The EEC Merger Regulation, Chapter 10; *Löffler*, in Langen/Bunte, Kartellrecht, Art 2 FKVO, Rn. 12-37.

165 Sec. 22 (3) No. 1 GWB. See Chapter 7.5.2. at pp. 327.

cent either in the common market or in a substantial part of it."

In the first decision blocked, *Aérospatiale-Alenia/de Haviland (1991)*,¹⁶⁶ which concerned the aerospace industry, in particular the market for regional turbo-prop aircrafts, the concentration would have resulted in a market share increase, even if the parties' definition of the relevant product market was accepted,¹⁶⁷ from 29 to 50 per cent world-wide and 49 to 65 per cent Community-wide. The remaining competitors being relatively weak and potential new entry into the market unlikely, the concentration was held to create a dominant position.

The second concentration blocked, *MSG Media Service (1994)*,¹⁶⁸ concerned three segments of the wider Pay-TV market in Germany. As this creation of a joint venture, *MSG*, by the two leading German media groups, *Bertelsmann* and *Kirch*, and the monopoly cable-provider, *Deutsche Telekom*, would have led to a virtual monopoly and forclosure of the German Pay-TV market, the concentration was considered to create or strengthen a dominant position in this new developing market.

The third prohibition again concerned the creation of a joint venture, *Nordic Satellite Distribution (1995)*, between three Scandinavian telecommunication groups, *Norsk Telekom* of Norway, *Tele Danmark*, and *Kinnevik* of Sweden.¹⁶⁹ Although the Commission welcomed in principle the cross-border co-operation as it could further technical progress (see Article 2 (1)(b)), the concentrative joint venture was nevertheless blocked as it would have created a highly vertically integrated group leading to, inter alia, a monopoly situation in the (up-stream) market for the distribution of

166 *Aérospatiale-Alenia/de Haviland* (2.10.91), [1991] O.J. L 334/42.

167 Namely of 20 to 70 seat commuter aircraft. The Commission found two different markets: (1) commuter aircraft of 40 to 59 seats: 64 % world-wide, 72 % Community-wide. (2) commuter aircraft of 60 seats and above: 76 % world-wide, 74 % Community-wide.

168 *MSG Media Service* (9.11.94), [1994] O.J. L 364/1. An Art 9 request by the German government was rejected in this case.

169 *Nordic Satellite Distribution*, [1996] O.J. L 53/10.

satellite frequencies for Scandinavia and a dominant position in the (down-stream) Scandinavian Pay-TV market.

In the last concentration blocked, *RTL/Veronica/Endemol* (1995),¹⁷⁰ which was referred to the Commission by the Netherlands under Article 22, the creation of the concentrative joint venture *Holland Media Groep* would have resulted in market shares of 56 to 63 per cent in the Dutch market for TV-advertising. In addition, despite a relatively low market share of only 50 per cent in the market for independent in-house TV-productions, *Endemol* would have gained a dominant position in this market due to a high degree of vertical integration (*Holland Media Groep* basically guaranteed to buy the *Endemol*-productions).

Various other concentrations which resulted in high market shares were not blocked. In *Tetra Pak/Alfa-Laval* (1991),¹⁷¹ for example, *Tetra Pak* held a market share of more than 90 per cent. Although the Commission found that *Tetra Pak* enjoyed a dominant position, the concentration was not blocked as it would not have led to a strengthening of that position: *Tetra Pak* was active in the market for liquid food packaging systems while *Alfa-Laval* operated in the food processing equipment industry. Another example is *Mannesmann/Hoesch* (1992)¹⁷² concerning the German market for steel tubes where the concentration led to a market share of over 70 per cent in the relevant market. Yet, the concentration was not blocked because of the potential (foreign) competition expected in this market by the Commission. The *KNP/BT/VRG* (1993)¹⁷³ concentration which created an enterprise controlling more than two-thirds of certain segments of the Dutch and Belgian printing press market was cleared after undertakings remedying some of the anti-competitive effects were given. An interesting case is

170 *RTL/Veronica/Endemol*, [1996] O.J. L 134/33.

171 *Tetra Pak/Alfa-Laval*, [1991] O.J. L 290/35.

172 *Mannesmann/Hoesch*, [1992] O.J. L 114/34.

173 *KNP/Bührmann Tetterode/VRG*, [1993] O.J. L 217/35.

Kali+Salz/MdK/Treuhand (1993)¹⁷⁴ because in this case the “*failing firm defence*” was invoked successfully. In this case the West-German company *Kali+Salz*, which had a 79 per cent market share of the fertiliser-potash market, took over the bankrupt East-German *MdK* company which led to an aggregate market share of 98 per cent. However, as *Kali+Salz* would have picked up the business of *MdK* anyway, the concentration was cleared.

These few examples may suffice to demonstrate that the Commission handles the market share criterion in a rather flexible way which is clearly more lenient than the approach taken by the German FCO under the GWB and more in line with the flexible British approach. Even high market shares exceeding 60 per cent do not necessarily result in a blocking of the concentration. On the basis of the cases so far decided by the Commission it would seem that concentrations leading to relatively low market shares below about 40 per cent would - at present - only in very exceptional cases risk prohibition. Because of Recital 14 of the Preamble, it can practically be outruled that a concentration resulting in a market share of less than 25 per cent would be prohibited.¹⁷⁵

8.4.2. Remaining Competitors

In order to assess whether the new combined entity would be able to act to an appreciable extent independently of its competitors, it is necessary to examine the market position of those competitors in terms of market shares, size and resources. Broadly speaking, the larger the gap between the merging firms and the next largest competitor, the greater the likelihood of a finding of market

174 *Kali+Salz/MdK/Treuhand*, [1994] O.J. L 186/38.

175 See also *Drauz/Schröder*, *Praxis der europäischen Fusionskontrolle*, p. 111; *Jones/González-Díaz*, *The EEC Merger Regulation*, pp. 133.

dominance. This approach is methodically in line with that of the British¹⁷⁶ and German¹⁷⁷ merger control authorities.

In *Aérospatiale-Alenia/de Haviland (1991)*¹⁷⁸ the Commission analysed in great detail the position of the remaining competitors and concluded that *“the competitors in these markets are relatively weak. The bargaining ability of the customers is limited. The combination of these factors leads to the conclusion that the new entity could act to a significant extent independently of its competitors and customers, and would thus have a dominant position on the commuter markets as defined.”*¹⁷⁹

Two further examples may suffice to demonstrate the Commission's approach. In *Magneti-Marelli/CEAC (1991)*,¹⁸⁰ which was finally cleared with conditions and obligations under Article 8 (2) of the Regulation, the Commission argued that the merging enterprises would attain a dominant position in the French market for starter batteries as *“the market share of the new entity would amount to some 60 % in France”* and *“the gap in relation to the next largest competitor would be considerable (of the order of 40 %)”*. In another battery case, *Varta/Bosch (1991)*,¹⁸¹ which was also declared compatible with the common market subject to conditions and obligations under Article 8 (2), the Commission reasoned in its statement of objections that *“in addition to the market share of 44 % and the lead of about 25 % over the next competitor, particular account was taken of the fact that the next competitors for the new entity in terms of market share were small and medium-sized companies with far less financial strength and smaller production capacity.”*

176 See Chapter 6.4.1.(2) at pp. 249.

177 See Chapter 7.5.1.(1) at pp. 323.

178 *Aérospatiale-Alenia/de Haviland* (2.10.91), [1991] O.J. L 334/42.

179 *Aérospatiale-Alenia/de Haviland* (2.10.91), [1991] O.J. L 334/42, para 51.

180 *Magneti-Marelli/CEA*, [1991] O.J. L 222/38, para 16.

181 *Varta/Bosch*, [1991] O.J. L 320/26, para 58.

8.4.3. Economic and Financial Power

Article 2 (1) (b) of the Regulation mentions among other criteria to be taken into account by the Commission *the economic and financial power* of the merging firms. Although the Commission has taken this factor into consideration at various times, it has not gained the crucial weight it has under German law.¹⁸² This might have to do with the fact that the German “*deterrence-doctrine*”, which is the dogmatic basis for the importance attributed to the financial strength criterion, has apparently not been adopted by the Commission.

In *Matsushita/MCA* (1991),¹⁸³ for example, a case which concerned the market for audio and video equipment, the Commission stated that “*the most important aspect of the proposed concentration is the possibility that the combination of the massive resources of MEI with the market position of either party might create considerable competitive advantages.*” However, the concentration was cleared unconditionally under Article 6 (1) (b) as sufficient competition remained.¹⁸⁴

8.4.4. Barriers to Entry and Potential Competition

Barriers to entry of new competitors are frequently considered by

182 At to German law see Chapter 7.5.1.(1)(b) at pp. 323.

183 *Matsushita/MCA*, CMLR 4 [1992] M36.

184 The financial strength was also taken into account in *Accor/Wagon Lits*, [1992] O.J. L 204/1 para 17; *Magneti-Marelli/CEA*, [1991] O.J. L 222/38, para 16: “*in addition, the financial strength of the new entity and that of its parent companies, and its greater access to the lead market, would also have to be taken into consideration.*”

the Commission. These may consist of intellectual property rights,¹⁸⁵ high costs involved or the need to achieve economies of scale in order to operate competitively, technological advantages in terms of research and development,¹⁸⁶ consumer preferences, brand loyalty or advertising costs¹⁸⁷ and so forth. Connected with entry barriers is the actual likelihood of new entry by potential competitors which is regularly considered by the Commission by way of a - necessarily uncertain - prognosis.¹⁸⁸

In *Tetra Pak/Alfa-Laval* (1991)¹⁸⁹, for instance, the Commission reasons: *"Although the Commission has identified at least one potential entrant it considers that the barriers to entry are sufficiently high to prevent that, and other, potential entrants from significantly limiting Tetra Pak's freedom of action... The reasons for this view are as follows: - Tetra Pak owns many patents useful for the production of an aseptic carton packaging machine. These valuable patents are not available to other potential entrants..."*

185 *Tetra Pak/Alfa-Laval*, [1991] O.J. L 290/35.

186 *Aérospatiale-Alenia/de Haviland* (2.10.91), [1991] O.J. L 334/42.

187 *Nestlé/Perrier*, [1992] O.J. L 356/1.

188 For a thorough analysis see for example *Aérospatiale-Alenia/de Haviland* (2.10.91), [1991] O.J. L 334/42 paras 53-63, at 63: *"It follows that there is no realistic significant potential competition in the commuter markets in the foreseeable future. The markets in the early 1990s, in contrast, are characterized by the following factors:*
- there are eight competitors altogether already on the markets. The aircraft available are all based on modern technology which fulfils the stringent customer requirements in this respect for the foreseeable future,
- current forecasts as outlined above show that the markets are approaching maturity and will decline and stabilize from the mid-1990s,
- the markets are not therefore attractive to new entrants, and it is not rational to now enter. The expectation is rather that some of the existing competitors will leave." See also *Mannesmann/Hoesch*, [1993] O.J. L 114/34 where the concentration in the steel tube sector was cleared despite a finding of market dominance due to a market share on the German market exceeding 70 % because the Commission considered it highly likely that new foreign competition would enter. For a more detailed analysis of this aspect see *Löffler*, in *Langen/Bunte*, *Kartellrecht*, Art 2 FKVO, Rn. 69.

189 *Tetra Pak/Alfa-Laval*, [1991] O.J. L 290/35 at para 3.4.

8.4.5. Other Criteria

A number of additional factors may be taken into account by the Commission, in particular vertical elements such as the access to supply or sales markets,¹⁹⁰ and countervailing purchasing power.¹⁹¹ As in Britain and Germany, these criteria are regularly confined to a contributory function. Industrial policy as opposed to competition considerations have apparently not gained significant weight.¹⁹² There is at least no reference to such considerations in the published decisions.

8.5. Concluding Remarks

Although the Merger Regulation contains elements of both British and German law, it is very much a distinct set of rules with a character of its own and is not closely modelled on either national law.

Politically, the most controversial issue has always been the demarcation of jurisdiction between the Community and the national merger control authorities which is nowadays reflected in the discussion on the reduction of the *Community dimension* thresholds. Firmly based on the *one-stop shop principle* designed to avoid multiple filings and conflicting decisions, the Merger Regulation provides for a clear and simple, albeit somewhat crude, jurisdictional

190 ICI/Tioxide, [1990] O.J. C 304/27; Viag/Continental Can, [1991] O.J. C 156/10. Mitsubishi/UCAR, [1991] O.J. C 5/7.

191 Alcatel/Telettra, [1991] O.J. L 122/48. For a detailed analysis see Nordemann, Buying Power and Sophisticated Buyers in Merger Control Law: The Need for a more Sophisticated Approach, [1995] 5 ECLR 270-281.

192 See Jones/González-Díaz, The EEC Merger Regulation, pp. 162; Löffler, in Langen/Bunte, Kartellrecht, Art 2 FKVO, Rn. 79.

test based on turnover thresholds. Due to the simplicity of this test and the present height of the thresholds there is relatively little scope for jurisdictional conflicts between the Commission and Member States. This is a remarkable achievement by the Regulation. Yet, concentrations not having a *Community dimension* in terms of the thresholds required may in fact have serious anti-competitive effects affecting competition in the common market. Vice versa, not every concentration meeting the substantial threshold requirements obstructs cross-border competition. The German and Dutch Clauses introduced to refine the somewhat simplistic threshold test are, however, used restrictively by both the Commission and the Member States, except Germany. However, the mentioned shortcomings of the threshold test have so far not been felt so much by the Member States and the companies involved as the thresholds are as a result of a political compromise rather high and the merger control regime exercised by Brussels is relatively lenient anyway. However, if the thresholds are reduced either nominally by the Council or creepingly in the long run due to inflation, it is submitted that the scope for jurisdictional conflict will increase as the jurisdictional reach of Commission expands; in particular the German Clause (referral to a Member State) will then be invoked more often. The *Alcatel/AEG Kabel* (1991) case has shown that there is a real potential for conflict.¹⁹³

The second pillar of the jurisdictional test, the definition of a concentration has been proved to be narrower with respect to minority holdings than the merger definitions applied in the U.K. and Germany. This may lead to the somewhat inconsistent result, that the acquisition of a substantial minority stake having a *Community dimension* may, because it does not constitute a concentration as defined by the Regulation, not be assessed by the Commission. Hence, despite having a *Communtiy dimension* these transactions

193 *Alcatel/AEG Kabel*, [1992] O.J. C 6/23 = CMLR 4 [1992] 80 = WuW/E EV 1713, 1714. See Chapter 8.3.3.(1) at pp. 370.

remain subject to (multiple) national merger control. A more uniform concentration/merger definition in the European Union appears therefore desirable in the long run. Although the *national* merger definitions could be harmonized by way of a new Directive, it is doubted whether this is necessary at present as the definitional divergencies have so far apparently not caused any major trouble. An easier option would be to expand the jurisdictional reach of the Merger Regulation, which is directly applicable within the Member States, so that any discrepancies between national merger definitions would be less felt in practice. Yet, this would mean to further reduce the role played by the national merger control authorities which does not appear to be politically opportune at present. There seems to be a tendency that the Commission in interpreting the concentration definition of the Regulation is moving closer to the broad merger concepts applied in Britain and Germany which basically means that the Commission is widening its definition and, thus, extends its jurisdictional reach creepingly.

Concerning the extra-jurisdictional scope of the Regulation the turnover-test applied is highly practicable, but far too undeveloped to really filter out those concentrations involving non-EC corporations which affect the common market. A comparison with the much more flexible and far broader criteria applied under British and German law underlines this point. Yet, whichever solution is found, the extraterritorial application of merger control law will always be a problem.

As to the institutional framework, the Merger Regulation differs from both British and German law. In common with the U.K. system, where only the Secretary of State for Trade and Industry may block a merger, under the Regulation the final decisions are also taken by a political institution: the college of Commissioners. This has been criticised above insofar as all Commissioners - including those who are no experts on competition law and policy - are involved. In this respect, British law differs as thereunder only the Secretary of State

for Trade and Industry and not the whole cabinet is charged with the decision-taking. It is submitted that the European merger control regime would gain credibility if the position of the Competition Commissioner was strengthened parallel to the situation in Britain so that he would become responsible for taking merger decisions rather than the full Commission. The German idea of an independent European competition authority modelled on the FCO in Berlin seems too far-reaching, unnecessary at present, and politically unrealistic.

In terms of substantive law, the European Merger Regulation is relatively closer to German law as it applies the test of market dominance whereas in Britain the broader public interest concept prevails. In applying the various criteria used to assess market dominance, which do not differ fundamentally from the competition criteria applied in Britain and Germany, the approach taken by the Commission is rather flexible. In particular the market share criterion is, as in Britain, treated with a high degree of flexibility sharply contrasting with the German approach which is, partly due to legal presumptions (33 per cent threshold), rather focused on market shares. The general perception of the business community, namely that European concentration control is more lenient than German merger control, appears to be correct. With respect to Britain, a similar statement can not be made.

PART FOUR

Summary

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Chapter 9

TAKEOVER REGULATION AND BARRIERS

The comparison of takeover regulation and barriers in Britain and Germany has contrasted two fundamentally diverging regulatory systems. The British regime governed by the City Code and administered by the Takeover Panel is well established and has been in operation for almost three decades the Panel having handled more than 6.000 announced takeover bids. Compared to this wealth of experience in Britain, the German takeover environment is still very much in its infancy with virtually no “real” Anglo-style (hostile) public takeover bids. Not surprisingly, thus, a proven regulatory framework for public takeover offers does not exist in Germany. The newly introduced voluntary German Takeover Code 1995 might be a first (controversial) step into the right direction, but lacks an efficient enforcement mechanism.

Various factors both legal and cultural have been identified causing this antagonistic situation thwarting the concept of a “level playing field” in the common market. While the British market for corporate control is by and large open to foreign bidders who are willing to act within the regulatory framework of the City Code, German stock corporations, albeit not impregnable, are difficult prey.

To begin with, compared to Britain the German securities market is rather underdeveloped due to a different corporate finance tradition relying more on debt rather than equity financing. Hence, the number of suitable listed stock corporations with widely dispersed shares is comparatively small. Non-listed stock

corporations or limited companies do not normally qualify as targets as they are often either owned by few investors, typically a family, or are part of a (closed) corporate group and the transfer of shares is often made conditional upon the consent of all shareholders.

Moreover, the organisational structure of German stock corporations as provided for in the Stock Corporations Act 1965 and ancillary employment Acts is not conducive to a functioning market for corporate control. Unlike British public companies where the shareholders may remove a director before the expiration of his period of office by ordinary resolution, notwithstanding anything in the articles or in any agreement between the company and him, the two-tier board system in Germany makes things far more complicated. First of all, there is no direct right for the shareholders to dismiss the members of the management board, who effectively run the company. The shareholders may only dismiss the members of the supervisory board, a three-quarter majority usually being required, and it is then within the supervisory board's discretion to dismiss the members of the management board the underlying concept being the independence of the management board. Although the two-tier board system prevents a bidder having the required majority from immediately installing its own management, he would succeed in the long run. Nevertheless, though, the two-tier board system clearly hampers takeover bids. A drawback of the German system is that as a result of the high degree of independence from shareholders enjoyed by the management of a German stock corporation together with the absence of any risk of being fired, the management may not perform as efficiently and effectively as the shareholders as owners of the company might wish. Short-termism, however, an evil often complained about in connection with the British industry, as a result of the permanent pressure on the management to content shareholders financially with high dividends as opposed to long-term investment, is effectively prevented by the two-tier board system making the management to a

large extent independent from such pressure. The German two-tier board system clearly promotes long-term strategic planning and investment, a feature that has certainly contributed considerably to the relative success of German industry in the postwar period. To some extent, short-termism appears to be the price to pay for the benefits of a functioning market for corporate control. Put simply, in terms of corporate governance, Britain and Germany appear to represent two almost diametrically opposed models at an extreme: management discipline and efficiency through a functioning market for corporate control versus long-term strategy and investment through management independence from short-term shareholder pressure.

In addition to the two-tier board system, another corporate governance feature to that degree unknown in English company law is the extensive employee representation and co-determination on supervisory board level guaranteed by German company and labour law. Again, this is no hard barrier preventing a bidder from winning control, but a factor making corporate governance at the post-acquisition stage more complicated and rendering German stock corporations less attractive to (foreign) bidders. Obviously, the structure of German stock corporations, in particular the division of power between shareholders, management and employees, is no barrier specifically erected to scare off (foreign) takeover bids, but a feature which has developed over decades as an intrinsic part of the corporate and political culture in Germany the consequence being that there is little prospect of any rapid change neither on national level nor through European initiatives.

Another aspect with both legal and cultural implications on which the respective takeover environments in the U.K. and Germany differ substantially is the role of the banks. Due to a certain corporate financing tradition in Germany (close housebank relationship together with frequent bank representatives on supervisory boards of German blue chip companies), a number of legal provisions

patronizing the banks (restricted voting rights in combination with proxy voting by banks), together with the absence of stringent disclosure provisions and the fact that German banks often hold significant stakes in German stock corporations resulting in a rather non-transparent thicket of mutually supportive holdings and interlocks, German banks enjoy a uniquely powerful position. One of the major German banks opposing a (foreign) takeover bid would therefore constitute a major problem for any bidder. Unlike the corporate structure of German stock corporations there are, however, indications that the situation regarding the role of the banks will change slowly. The Securities Trading Act 1994, partly based on European Directives, has introduced relatively stringent disclosure provisions regarding listed stock corporations and the traditional housebank relationship might in times of increased competition in the banking sector lose some of its importance. The need for making the German securities market more open and transparent in order to win investor confidence and strengthen the competitive position of Germany as a financial centre has clearly been recognized by government and industry leaders as the "Finanzplatz Deutschland" campaign shows. It is very likely that in the next years legislation will be introduced restricting the power of banks. A legislative measure overdue, for example, is the abolition of restricted voting rights for listed stock corporations. Restricted voting rights are clearly intended to protect the incumbent management against shareholder pressure and boost the banks' power through their proxy votes.

Present developments on European level, however, can not be expected to really further the idea of a level playing field for takeover bids. The newly proposed Takeover Directive 1996, being the result of a political compromise, is far too vague to bring about any tangible change. Neither does it provide for a sufficiently precise takeover procedure nor an imperative mechanism designed to protect minority shareholders. Such a Directive having little more than an alibi function is simply unnecessary. Pursuant to the European principle

of subsidiarity, it is submitted that the Commission should shelve the proposal for a Takeover Directive until a genuine consensus is found and, more importantly, until there is a real need for a Takeover-Directive. Clearly, with respect to Germany where inherent structural barriers effectively prevent or at least discourage public takeover bids it is difficult to see why a Directive providing for a takeover procedure and the protection of minority shareholders should do anything in terms of promoting a level playing field. Such a Directive makes sense only where there is already a takeover bid activity which needs to be regulated. Germany has not reached that stage yet. Concerning Britain, there is, of course, intensive public bid activity. But Britain has a well functioning regulatory framework and there is therefore equally little reason to believe that the U.K. should need the proposed Takeover Directive.

It is submitted that what is needed are further efforts on European and national level to lessen the more structural barriers which obstruct cross border acquisitions. The proposed Fifth Directive contains some very useful measures to that effect, like the curtailment of voting right restrictions as installed by some listed German Stock Corporations. However, there appears to be little movement in that direction the proposed Fifth Directive remaining blocked for political reasons. Some of the barriers identified, however, like the two-tier board system and employee representation, are manifestations of the corporate-industrial culture in Germany and can for political reasons not simply be abolished by any legislative measure nor is this wanted in Germany. As the idea of a regulation providing for a European Company (*Societas Europaea*) is not on the agenda any more, the only real chance of a level playing field for takeovers will in the very long run come from slow change forced by increasing international competition and market pressure in the financial sector.

Chapter 10

MERGER CONTROL

Merger control is a young field of law very much in a state of flux. It is inherently inexact and somewhat speculative as it is entirely based on a most complex prognosis as to how markets will develop in future as a result of a (proposed) merger. This prognosis is all the more difficult where international factors come into play which might be difficult to properly assess for a national or even European authority. Potential market entry, for example, is something nobody really can foresee. Although this thesis concentrates on the legal technicalities of merger control and deliberately avoids the fundamental economic question whether merger control makes sense at all, given the inherent inadequacies of merger control law this seems a question worth thinking about. Maybe market forces and the ability to prevent abuses of market power would suffice to guarantee sufficiently open and competitive markets. However, this is an issue clearly not on the agenda at present.

The regulatory scene in Britain and Germany is characterized by the coexistence of national rules, which apply to “*national*” mergers, and the directly applicable European Merger Regulation, which is applicable where a concentration has a “*Community dimension*”. The analysis has shown that the national merger control regimes of Britain and Germany reflect the different legal cultures in which they have developed. This is most evident with respect to the institutional frameworks of merger control. In Britain, where three institutions are charged with policing mergers, mergers may be blocked by the Secretary of State for Trade and Industry only, hence, ultimately by a political institution. Thus, merger control is to some degree seen as a

means to shape industrial policy and therefore contains a political element. In Germany, it is distinctly seen as an administrative affair almost exclusively in the hands of the independent Federal Cartel Office and the courts, which are heavily involved in the merger control process as virtually no blocking decision remains legally unchallenged.

This different approach to merger control is also mirrored in the substantive appraisal criteria. In the U.K. the relevant substantive criterion against which mergers are assessed is the *public interest*. This criterion is highly flexible allowing the merger control authorities to take into account all matters which appear to them in the particular circumstances to be relevant. Although, in line with German and European law, competition is by far the single most important public interest criterion taken into account by the U.K. authorities. The German Federal Cartel Office and the German courts strictly focus on the question whether the merger may be expected to result in the creation or strengthening of a dominant position. Their flexibility is further restricted by the weight attributed to the *market share* the merging enterprises are expected to attain by way of legal presumptions (33 per cent presumption) contained in the Act against Restraints of Competition. Merger control in Germany is therefore comparatively inflexible and rigid on the one hand, but rather predictable on the other. In Britain, the opposite tends to be true.

In theory, there is no jurisdictional overlapping between the national and the European merger control authorities: the one-stop shop principle applies pursuant to which Brussels has access only to those *concentrations* which have a *Community dimension*. It has been demonstrated that the jurisdictional demarcation based on turnover thresholds set up by the Merger Regulation is rather simplistic and that there is a potential for jurisdictional conflict. However, any shortcomings of the Regulation in that respect have so far been easy to take for anybody involved as the current *Community dimension* thresholds are deliberately set at rather high level which

ensures that only relatively few concentrations come within the reach of the Merger Task Force at the Directorate General IV and the merger control regime exercised in Brussels has been rather lenient - too lenient as many in Germany claim. However, at least the relative importance of the Merger Task Force is probably going to grow in the long run. Although it seems unlikely for political reasons that the EC-Commission will succeed with its proposal to formally reduce the current thresholds, due to inflation, the enlargement of the European Union, and business transactions ever increasing in volume, more and more transactions will fall under the Regulation.

A key problem of any national merger control system these days is the growing internationalization of markets. This does not only lead to multiple national filings which carry the inherent risk of conflicting decisions by national merger control authorities. Moreover, the national merger control authorities are at best seriously challenged with policing such mergers. Simply not to allow a geographic market definition exceeding national borders, as both the U.K. and German merger control authorities do, means closing the eyes to the commercial reality and looks like a trick rather than a solution. As large multinational companies operate at an international or even global stage, the national authorities monitoring these transactions also have to have an international perspective and cross-border powers if they are to be taken seriously as a counterweight to the multinational companies. It has been demonstrated that "foreign" mergers may well affect the national market. However, for reasons of the public international law principle of non-intervention in foreign affairs, the hands of the national authorities are by and large bound. Although these fundamental issues have been recognized and the Merger Regulation tries to tackle the problem to some degree, it is submitted that the efforts do not go far enough and the proposed threshold reduction would be a first step into the right direction. On a national level it appears that there is a need to redefine the role of the national merger control authorities in the face of an increasingly

international business world. Clearly, to hand over power to Brussels is a measure highly unpopular with both Britain and Germany. However, unlike takeover regulation, merger control can not be properly exercised at a national level where international markets are concerned.

Appendix

German Takeover Code 1995

Takeover Code of the Stock Exchange Experts Commission*

INTRODUCTION

The Takeover Code is a set of recommended rules of conduct for parties involved in voluntary public takeover offers, which has been drawn up by the Stock Exchange Experts Commission. The Code is designed - without prejudice to any statutory rules - as a flexible instrument which can be adapted from time to time in accordance with practical experience. While not addressing the question of whether public takeovers are expedient, the Code is, nevertheless aimed at helping to ensure that public offers contain all the information necessary to enable a careful and properly informed decision to be made by the holders of securities and the boards of the relevant company (target). The Code is intended to prevent market manipulation and to ensure that all parties involved act in good faith. For this reason, the Code must be observed not only according to its letter but also according to its underlying purpose.

DEFINITIONS

Public Offers

Public Offers within the meaning of this Code are public purchase and exchange offers for cash or in consideration of other securities, as well as invitations to make offers, which are made by an offeror to the holder of securities in a target (other than in fulfilment of a legal obligation) with the intention of acquiring those securities at a fixed cash price or by way of exchange for other securities within the meaning of section 2 paragraph 1 of the Securities Trading Act (WpHG).

Offeror

Offeror within the meaning of this Code is any natural or legal person who alone or together with other persons, makes a public offer.

Target

Target within the meaning of this Code is any stock corporation (Aktiengesellschaft) or partnership limited by shares (Kommanditgesellschaft auf Aktien) with its corporate seat in Germany, the securities of which are the subject-matter of a public offer and are listed on a German stock exchange or have been included in the over-the-counter market (Freiverkehr) with the target's consent.

Securities

Securities within the meaning of this Code are all rights which the offeror is seeking to acquire and which directly or indirectly confer voting rights at the general meeting of the target. These include ordinary shares, shares with enhanced voting rights and those preference shares which

* This translation relies on a translation obtained from the *German Takeover Panel* which was prepared by law firm *Freshfields*. Only the German version is authoritative.

carry voting rights at the time of the announcement of the offer, as well as substitutes for such securities (e.g. American Depositary Receipts, ADRs). Rights to subscribe for those shares which can be newly created by a unilateral declaration on the part of the holder of the right are also securities within the meaning of this Code. The Code also applies to offers to acquire securities resulting from an issue which have been neither admitted to trading on a stock exchange nor included in the over-the-counter market (*Freiverkehr*), if other securities resulting from the same issue are traded on a stock exchange.

If a public offer is made for non-voting preference shares, the rules of the Code shall apply by way of analogy.

Takeover Panel

The member of the Takeover Panel will be appointed by the Commission of Stock Exchange Experts Commission. The Takeover Panel will mainly be responsible for the resolution of disputes.

Executive

The Executive of the Takeover Panel is its executive arm. The Executive is responsible for monitoring compliance with the Code.

GENERAL PRINCIPLES

Article 1

In the course of a public offer, the offeror must treat all holders of securities of the same class equally.

Article 2

The offeror and the target must provide all holders of securities which are the target of the public offer with the same information needed to evaluate the offer. The information must be accurate and stated in an appropriate manner. This applies not only to the information set out in Article 7 but also to any additional information given, irrespective of whether it is contained in the offer itself or otherwise made public by the offeror or the target.

Where a public offer has been made, the management board (*Vorstand*) of the target is obliged, upon proper exercise of its discretion and in the interests of the holders of securities, to make such information as has been made available to the original offeror also available to any other persons who have demonstrated a genuine interest in taking over the target. The Takeover Panel shall determine, upon application by the target, whether or not such interest is genuine.

Article 3

During the offer period the offeror and the target must refrain from doing anything which could result in unusual changes in the market price of securities of the target or securities which are being offered in exchange for securities of the target. In particular, statements should be avoided which could mislead the holders of securities of the offeror or of the target or which could mislead the market.

Article 4

The announcement of an offer should generally be preceded by consultations between the offeror and the target.

Article 5

Prior to making a public offer, the offeror must inform the target, the German stock exchange on which the securities of the target and, where applicable, the securities offered in exchange are listed, the Federal Supervisory Office for Securities Trading and the Executive of the Takeover Panel as to the content of the offer and thereafter publish the offer without delay in at least one national journal for mandatory stock exchange notices (*Börsenpflichtblatt*).

Article 6

For the purposes of the preparation and implementation of the offer the offeror shall retain the services of an undertaking authorised to provide investment services within the meaning of the EC Directive. This undertaking shall have either its seat or a branch in a member state of the European Union.

CONTENT OF THE OFFER**Article 7**

The offer must include at least the following:

1. name of the offeror and, where applicable, the undertaking retained pursuant to Article 6 of the Code;
2. name of the target;
3. the securities which are the subject-matter of the offer;
4. the maximum and/or minimum amount of securities which the offeror undertakes to acquire together with an explanation of the allotment procedure pursuant to Article 10;
5. information concerning the purchase price or other consideration and about the implementation of the offer;
6. information concerning the principal factor relevant to the determination of the consideration;
7. indication of whether the offer will be accepted upon the shareholder of the target declaring his acceptance or whether the shareholders of the target are merely being invited to offer securities of the target to the offeror;
8. information concerning timing and concerning the amount of securities of the target acquired by the offeror prior to the offer and any contracts entered into in respect of such securities but not yet performed;
9. where applicable, information concerning direct and indirect holdings of the target in the offeror (to the extent known);
10. any statement made by the target;
11. the offer period;
12. any conditions attached to the offer and any right of withdrawal reserved by the offeror;
13. information concerning the aims and intentions of the offeror in relation to the target and the possible effects of a successful offer, in particular with regard to the financial situation

of the offeror and the target;

14. notice of the effecto that holders of securities of the target have a right to withdraw from the acceptance of the offer pursuant to Article 14;
15. notification of the date on which the result of the offer will be published;
16. indication of the progress of any merger control procedure (if applicable);
17. notice of any dispensation granted by the Takeover Panel from provisions of this Code (if applicable);
18. undertakings by the offeror to comply with the provisions of this Code.

Article 8

Any announcement addressed to holders of securities of the target shall be prepared with the highest standards of care and accuracy.

Article 9

The offer may only be made subject to conditions the fulfilment of which cannot be brought about by the offeror itself. In case of doubt, the conditions should be cleared with the Executive.

Article 10

If the number of securities held by holders of securities accepting the public offer is higher than the number of securities which the offeror has undertaken to acquire, the acceptances by holders of securities must be scaled down on a pro rata basis.

Article 11

The offeror must give the holders of securities which are the subject-matter of the offer an appropriate period of time to consider the offer and come to a decision. The offer period must be at least 28 days but no more than 60 days.

DUTIES OF THE OFFEROR

Article 12

Following the announcement of its public offer, the offeror is obliged, by the following business day, to notify the Executive and to publish all dealings (number, price) in securities of the target which have been carried out by it for its account following announcement of the public offer. This duty also applies to dealings in securities within the meaning of section 2 paragraph 1 of the Securities Trading Act if such securities are offered in exchange for securities of the target. It does not apply to the acquisition of shares in reliance on section 71 paragraph 1 No. 2 of the Stock Corporation Act.

Article 13

If the offeror acquires securities of the target during the offer period on more favourable terms than those set out in the offer, the more favourable terms shall apply to all holders of securities of the same class even if they have already accepted the public offer.

Article 14

The offeror may, within the offer period, make an offer which is more favourable to the holders of securities of the target - in particular if, following publication of the offer pursuant to Article 5, more favourable offers for the purchase of the relevant securities of the target are made by third parties. In such a case, the offeror may extend the original offer period by a period cleared with the Executive. If the offeror makes use of this right, it must ensure that all holders of securities who have already accepted the offer are (retrospectively) treated equally. Such holders of securities shall have the right to withdraw from the offer already accepted in order to accept the more favourable offer.

Article 15

If during a period to be specified by the offeror in the offer, which period must not be less than 12 months, a more favourable voluntary offer is made by the offeror, and if during this period no offer is made by a third party, then the offeror must also make the more favourable offer available to those who accepted the initial offer.

Article 16

If, following the entry into force of this Code, a holder of securities comes to hold more than 50 per cent of the voting rights in a target (including voting rights which are deemed to be held by him pursuant to section 22 paragraph 1 of the Securities Trading Act) (majority shareholder), as a result of acquisitions on or off the stock exchange, and if, within a period of 18 months from the date on which this threshold has been exceeded, neither the target nor the majority shareholder has passed resolutions for:

- an enterprise agreement with the target in accordance with sections 291 et seq. of the Stock Corporations Act;
- the integration of the target in accordance with sections 319 et seq. of the Stock Corporations Act;
- a change of the legal form of the target in accordance with sections 190 et seq. of the Conversion Act (Umwandlungsgesetz);
- the merger of the target with the majority shareholder in accordance with sections 2 et seq. of the Conversion Act;

then the majority shareholder shall within a further period of three months make an offer to all other holders of securities of the target for the acquisition of the remaining securities (mandatory offer).

A mandatory offer is dispensable:

- if the 50 per cent threshold was exceeded by virtue of securities which the majority shareholder holds only for an interim period for the purposes of placing them with third parties;
- in the event that the majority shareholder unintentionally acquires more than 50 per cent of the voting rights of the target and without delay reduces his share in the voting rights to 50 per cent or less;
- if, within a period of 18 months following the date on which the 50 per cent threshold was exceeded, the majority shareholder has been released by the general meeting of the target, from the obligation to make a mandatory offer and has prior thereto confirmed in writing to the Executive that he will not exercise his voting rights when this item of the agenda is voted upon.

Voting rights attaching to securities which are held for dealing purposes and for which an exemption has been granted by the Federal Supervisory Office for Securities Trading under section 23 paragraph 2 of the Securities Trading Act shall not be taken into account.

Article 17

If, after exceeding the 50 per cent threshold and prior to making the mandatory offer, a majority shareholder has not made any further purchases of securities of the target, the price offered in the course of the mandatory offer must reasonably reflect the then current market price. It shall not be more than 25 per cent below the price which the majority shareholder paid for securities of the target in the six month period prior to the passing of the threshold.

If, after exceeding the 50 per cent threshold and prior to making the mandatory offer, a majority shareholder has made further purchases of securities of the target, the weighted average price paid in the course of such purchases shall, provided that it is higher than the price referred to in paragraph 1 above, be used as the basis for determining the price to be offered in the course of the mandatory offer.

These provisions shall apply by way of analogy if securities are offered by way of exchange.

DUTIES OF THE TARGET

Article 18

The target shall publish without delay - and, at the latest, within 2 weeks following publication of the offer - a reasoned statement of its position in relation to the offer.

Article 19

After the announcement of a public offer and prior to the announcement of the result of the offer, the administrative or executive boards of the target (including the administrative or executive boards of any company associated with the target) may not take any measures which conflict with the interests of the holders of securities in accepting the offer.

This applies inter alia to resolutions regarding:

- the issue of new securities;
- material changes to the assets or liabilities of the target; and
- the conclusion of agreements outside the ordinary course of business.

This shall not apply to ongoing capital measures or to the performance of contracts which had been entered into by the target prior to the announcement of the public offer or if the general meeting expressly authorises these measures to be taken in the event of a public offer.

TAKEOVER PANEL

Article 20

1. The Takeover Panel shall consist of at least seven but not more than fifteen members.
2. The members of the Takeover Panel, its Chairman and his Deputies, shall be appointed by the Stock Exchange Experts Commission.

3. The appointment will be made for a period of five years. A re-appointment is possible.
4. When deciding upon the composition of the Takeover Panel, particular regard should be had to the following groups:
 - issuers;
 - institutional investors;
 - private investors;
 - credit institutions and providers of investment services.
5. If a member of the Takeover Panel leaves, the Stock Exchange Experts Commission shall appoint a new member for the remaining term of office of the member who has left.
6. The Stock Exchange Experts Commission shall issue rules of management and procedure for the Takeover Panel and the Executive.
7. The Takeover Panel shall appoint the Head of the Executive Bureau.

Article 21

Potential offerors, targets and providers of investment services are asked to acknowledge the provisions of the Code. The Executive will regularly publish a list of those enterprises and persons who have acknowledged these provisions.

If this Code is contravened, the Executive may publish its comments, recommendations and decisions in relation to the particular case. Prior to publication, the Executive must grant the parties concerned a hearing. The parties concerned may then appeal to the Takeover Panel prior to publication and the Takeover Panel's decision shall be final.

Article 22

Within a period of two weeks following its announcement, the Executive shall examine whether or not a public offer complies with the Code. The offeror, the target and the enterprises involved pursuant to Article 5 shall give the Executive all information necessary for the supervision of, and compliance with, the Code.

Article 23

The Takeover Panel may (wholly or partly) release the offeror or the target from individual provisions of the Code if the application of such provisions would damage the legitimate interests of the offeror, the target or the holders of securities of the target. This applies, in particular, to the duty to make an offer pursuant to Article 16. Any decision regarding such release will be published, with reasons, by the Takeover Panel.

Article 24

This Code shall come into force on 1 October 1995.

Frankfurt, 14 July 1995

German Stock Corporation Act 1965^{*}

§ 12

Voting right. No multiple voting rights

(1) Each share gives the right to vote. However, under the provisions of this Act preference shares without a voting right may be issued.

(2) Multiple voting rights are not permitted. The highest competent authority for the economy of the state in which the association has its domicile may grant exceptions to the extent this is necessary to guard prevailing interests of the general economy.

§ 15

Connected enterprises

Connected enterprises are legally independent enterprises which in relation to each other constitute either enterprises held by a majority and enterprises holding the majority (§ 16), dependent and dominant enterprises (§ 17), group enterprises (§ 18), mutually participating enterprises (§ 19), or parties to enterprise contracts (§§ 291, 292).

§ 16

Enterprises held by majority and enterprises holding the majority

(1) If the majority of the shares in a legally independent enterprise belongs to another enterprise or if another enterprise is entitled to the majority of the voting rights (holding the majority), then such enterprise constitutes an enterprise held by a majority, and the other enterprise is an enterprise holding it with a majority.

(2) For (ordinary) corporations the portion of shares which belongs to an enterprise is determined by the ratio which the aggregate nominal amount of the participations belonging to it bears to the nominal capital, and for mining corporation by the ration between the number of the mining shares. Shares held in tis won enterprise shall be deducted, for (ordinary) corporations from the nominal capital, for mining corporations from the number of the mining shares. Shares in the enterprise belonging to another for the account of the enterprise are deemed to be equivalent to holding shares in its own enterprise.

(3) The portion of the voting rights to which an enterprise is entitled is determined by the ratio of the number of the voting rights which it may exercise from the shares belonging to it to the

For a complete translation of the of the German Stock Corporation Act 1965 refer to *Schneider/Heidenhain*, The German Stock Corporation Act, Kluwer Law International, 1996. See also *Müller/Galbraith*, The German Stock Corporation Law, 2nd edition 1976, Fritz Knapp Verlag, Frankfurt am Main. The translation contained in this Appendix is based on this text. A translation of the relevant provisions of the law of groups, §§ 291-328 of the Stock Corporation Act, can also be found in *Schmitthoff/Wooldridge*, Groups of Companies, London, 1991.

aggregate number of all voting rights. From the aggregate number of all voting rights there shall be deducted the voting rights from shares held in its own enterprise as well as from shares which are equivalent pursuant to subsection 2 sentence 3.

(4) In shares belonging to an enterprise there shall also be included shares belonging to an enterprise dependent on it or to another for the account of the enterprise or of an enterprise dependent on the latter and, if the owner of the enterprise is a single trader, also those participations which constitute other property of the owner.

§ 17

Dependent and dominating enterprises

(1) Dependent enterprises are legally independent enterprises on which another enterprise (dominating enterprise) is able to directly or indirectly exercise a dominating influence.

(2) It is presumed that an enterprise held by a majority is dependent on the enterprise holding the majority.

§ 18

Corporate group and group enterprises

(1) If a dominating and one or more dependent enterprises are joined by the uniform direction of the dominating enterprise, then they constitute a corporate group; the individual enterprises are group enterprises. Enterprises between which a contract of domination exists (§ 291) or if one of them is integrated into the other (§ 319) are to be considered as joined by a uniform direction. It is presumed that a dependent enterprise forms a corporate group with the dominating enterprise.

(2) If legally independent enterprises are joined by a uniform direction without the one enterprise being dependent on the other, then they also constitute a corporate group; the individual enterprises are group enterprises.

§ 19

Mutually participating enterprises

(1) Mutually participating enterprises are enterprises with a domestic domicile in the legal form of an (ordinary) corporation or a mining corporation which are connected in such a manner that each enterprise owns more than one fourth of the shares in the other enterprise. § 16 subsection 2 sentence 1, subsection 4 apply to the determination of whether or not an enterprise owns more than one fourth of the participations in the other enterprise.

(2) If one of the mutually participating enterprises holds a majority in the other enterprise or if one is able to directly or indirectly exercise a dominating influence on the enterprise, then the one is to be considered a dominating, the other a dependent enterprise.

(3) If each of the mutually participating enterprises holds a majority in the other enterprise or if each is able to exercise a dominating influence directly or indirectly on the other enterprise, then both enterprises are to be considered as dominating and as dependent.

(4) § 328 is not to be applied to enterprises which constitute dominating or dependent enterprises pursuant to subsections 2 and 3.

§ 20**Duty to disclose**

(1) As soon as an enterprise owns more than one fourth of the shares of a stock corporation with a domestic domicile it shall inform the association of this fact in writing without undue delay. § 16 subsection 2 sentence 1, subsection 4 apply to the determination of whether or not the enterprise owns more than one fourth of the shares.

(2) With respect to the duty to inform pursuant to subsection 1 there shall also be counted as shares belonging to the enterprise those shares

1. the transfer of ownership of which the enterprise, on an enterprise dependent on it, or another for the account of the enterprise or of an enterprise dependent on the latter, may demand;
2. which the enterprise, or an enterprise dependent on it, or another for the account of the enterprise or of an enterprise dependent on the latter, is obligated to take over.

(3) If the enterprise is an (ordinary) corporation or a mining corporation, then it shall also inform the association in writing without undue delay as soon as it owns more than one fourth of the shares, not including the shares pursuant to subsection 2.

(4) As soon as the enterprise holds a majority (§ 16 subsection 1) it shall also inform the association of this fact in writing without undue delay.

(5) If the participation no longer exists in the amount creating the duty to inform pursuant to subsections 1, 3 or 4, then the association shall be informed of this fact in writing without undue delay.

(6) The association shall publish the existence of a participation of which it has been informed pursuant to subsections 1 or 4 in the association's journal without undue delay; the enterprise to which the participation belongs shall be named therein. If the association is informed that the participation has ceased to exist in the amount creating the duty to inform pursuant to subsections 1 or 4 then this fact shall also be published in the association's journal without undue delay.

(7) Rights from shares which belong to an enterprise obligated to inform pursuant to subsections 1 or 4 may not be exercised for the period in which the enterprise has failed to give the information neither by the enterprise itself, nor by an enterprise dependent on it, nor by another for the account of the enterprise or of an enterprise dependent on the latter.

§ 21**Duty of the association to disclose**

(1) As soon as the association owns more than one fourth of the participations in another (ordinary) corporation or mining corporation with domestic domicile it shall inform the enterprise in which the participation exists of this fact in writing without undue delay. § 16 subsection 2 sentence 1, subsection 4 apply accordingly to determine whether or not the association owns more than one fourth of the shares.

(2) As soon as the association holds the majority (§ 16 subsection 1) in another enterprise it shall inform the enterprise in which it holds the majority of this fact in writing without undue delay.

(3) If the participation no longer exists in the amount creating the duty to inform pursuant to subsections 1 or 2, the association shall inform the other enterprise of this fact in writing without undue delay.

(4) Rights from participations which belong to an association obligated to inform pursuant to subsections 1 or 2 may not be exercised for the period in which it has failed to disclose the information.

§ 22

Evidence of the participations so communicated

An enterprise to which an information has been given pursuant to § 2 subsections 1, 3 or 4, § 21 subsections 1 or 2 may request at any time to be shown evidence of the existence of the participation.

§ 68

Transfer of nominative shares. Transcription in the share register

(1) Nominative shares may be transferred by indorsement. For the form of the indorsement, the evidence of the holder's title and his obligation to deliver articles 12, 13 and 16 of the Bills of Exchange law (Wechselgesetz) apply accordingly.

(2) The articles of association may make the transfer dependent on the consent of the association. The consent is granted by the board of management. The articles of association may determine the reasons for which the consent may be refused.

(3) If a nominative share passes to another person, then the association must be notified. The share must be submitted and evidence of the passing must be given. The association registers the passing in the share register.

(4) The association is obligated to examine the regularity of the chain of indorsements and of the declarations of transfer, but not the signatures.

(5) These provisions apply accordingly to interim certificates.

§ 76

Direction of the stock corporation

(1) The board of management shall direct the association as a matter of its own responsibility.

(2) The board of management may consist of one or more persons. In associations with a share capital of more than three million Deutsche Mark it shall consist of at least two persons unless the article of association determine that it shall consist of one person. The provisions regarding the appointment of a director of personnel remain unaffected.

(3) Only a natural and legally fully capable person may be member of the board of management. (*continues*)

§ 77

Management

(1) If the board of management consists of several persons, then all of the members of the board of management are authorized only to manage jointly. The articles of association or the rules of business of the board of management may determine otherwise; it may not however be determined that one or more members of the board of management may decide differences of opinion within the board of management against the majority of its members.

(2) The board of management may set up its rules of business unless the articles of

association have conferred upon the supervisory board the issuing of rules of business or the supervisory board issues rules of business for the board of management. The articles of association may regulate the rules of business in detail with binding effect. Resolutions of the board of management regarding its rules of business must be taken unanimously.

§ 78

Outside Representation

- (1) The board of management represents the association in and out of court.
- (2) If the board of management consists of several persons, then all members of the board of management are only authorized to represent the association jointly, provided the articles of association do not provide otherwise. If a statement with legal effect must be made to the association, making it to one member of the board of management suffices.
- (3) The articles of association may also determine that individual members of the board of management are authorized to represent the association solely or jointly with a *Prokurist*. The supervisory board may make the same determination, provided the articles of association authorize it to do so. Subsection 2 sentence 2 applies accordingly in these cases.
- (4) Members of the board of management authorized to represent jointly may authorize individual members among themselves to transact a certain business or certain kinds of business. This applies accordingly if an individual member of the board of management is authorized to represent the association jointly with a *Prokurist*.

§ 84

Appointment and removal of management

- (1) The supervisory board appoints members of the board of management for a maximum of five years. A renewal of the appointment or extension of the period of office is permissible, in each case for a maximum of five years. This requires a renewed resolution of the supervisory board which may be taken at the earliest one year before the expiration of the current term of office. An extension of the period of office may only be given, without a new resolution of the supervisory board, for an appointment for less than five years, provided the aggregate term of office does not thereby constitute more than five years. This applies accordingly to a contract of employment; however it may provide that it continues to apply in the case of an extension of the term of office until the term expires.
- (2) If several persons are appointed as members of the board of management, then the supervisory board may nominate a member as chairman of the board of management.
- (3) The supervisory board may revoke the appointment of a member of the board of management or the nomination as chairman of the board of management if there is a justified reason for doing so. In particular a gross violation of duties, incapability of proper management or withdrawal of confidence by the shareholders' meeting, unless the confidence has been withdrawn for obviously arbitrary reasons, constitutes such justified reason. This applies also to the board of management which was appointed by the first supervisory board. The revocation is effective until its ineffectiveness has been determined by a final court decree. For claims under the contract of employment, the general provisions of law apply.
- (4) The provisions concerning special majorities required for a resolution of the supervisory board regarding the appointment or removal of a labour-director contained in the Act of 21 May 1951 (Bundesgesetzblatt I. S. 347) concerning the co-determination of employees in the supervisory and management boards of mining and steel corporations (Montan-Mitbestimmungsgesetz) apply notwithstanding anything stipulated in the previous subsections.

§ 87**Principles for the compensation of members of the board of management**

(1) The supervisory board shall take care in determining the aggregate compensation of the individual member of the board of management (salary, profit sharing, compensations for expenses, insurance premiums, commissions and fringe benefits of any kind) in such a way that the aggregate compensation keeps within reasonable relation to the duties of the member of the board of management and to the situation of the association. This applies accordingly to pensions, payments to surviving dependents and consideration of a related kind.

(2) If after the determination a substantial deterioration of the associations situation occurs in such a way that the continuation of the compensation referred to in subsection 1 sentence 1 would constitute a grave inequity to the association, then the supervisory board, and the court upon motion of the supervisory board in the case of § 85 subsection 3, are authorized to make reasonable reductions. The contract of employment is otherwise not affected by a reduction. The member of the board of management may however terminate his contract of employment as of the end of the next calendar quarter year, with a period of notice of six weeks.

(3) If bankruptcy proceedings are instituted against the association's assets and if the receiver in bankruptcy serves notice to terminate the contract of employment of a member of the board of management, then such member may only claim the damage, arising out of the termination of the employment. The same applies if composition proceedings are instituted against the association and the association serves notice to terminate the contract of employment.

§ 93**Duty of diligence and liability of members of the board of management**

(1) In their management the members of the board of management shall employ the diligence of an orderly and conscientious manager. They shall keep secret the confidential statements and secrets of the association, especially trade and operational secrets which have become known to them from their service on the board of management.

(2) Members of the board of management who violate their duties are jointly and severally liable to the association for the resulting damage. If it is contested whether or not they have applied the diligence of an orderly and conscientious manager, then the burden of proof is on them. (*continues with subsections 3-6*)

§ 95**Number of members of the supervisory board**

The supervisory board consists of three members. The articles of association may determine a specific higher number. The number must be divisible by three. The maximum number of members of the supervisory board is for associations with a share capital

up to 3.000.000 Deutsche Mark at nine

of more than 3.000.000 Deutsche Mark at fifteen

of more than 20.000.000 Deutsche Mark at twentyone.

Deviating provisions of the Act of 21 May 1951 (Bundesgesetzblatt I. S. 347) concerning the co-determination of employees in the supervisory and management boards of mining and steel corporations (Montan-Mitbestimmungsgesetz) and of the Act to amend the law on co-determination of employees in the supervisory and management boards of mining and steel corporations of 7 August 1956 (Bundesgesetzblatt I. S. 707 Mitbestimmungsänderungsgesetz)

are not affected by the foregoing provisions.

§ 96

Composition of the supervisory board

(1) The supervisory board is composed

in associations to the the Co-determination Act (Mitbestimmungsgesetz) applies, of members of the supervisory board of the shareholders and of employee members,

in associations to which the Act of 21 May 1951 (Bundesgesetzblatt I. S. 347) concerning the co-determination of employees in the supervisory and management boards of mining and steel corporations (Montan-Mitbestimmungsgesetz) applies, the members of the supervisory board of the shareholders and of employee members and additional members,

in associations to which §§ 5 to 13 of the Co-determination Amendment Act (Mitbestimmungsänderungsgesetz) apply, of members of the supervisory board of the shareholders and of employee members and of one additional member,

in associations to which § 76 subsection 1 of the Works Constitution Act 1952 (Betriebsverfassungsgesetz) applies, of members of the supervisory board of the shareholders and of employee members,

in other associations only of members of the supervisory board of the shareholders.

§ 101

Appointment of members of the supervisory board

(1) The members of the supervisory board are elected by the shareholders' meeting unless they are to be named to the supervisory board or to be elected as employee members of the supervisory board pursuant to the Co-determination Act (Mitbestimmungsgesetz), the Co-determination Amendment Act (Mitbestimmungsänderungsgesetz), or the Works Constitution Act 1952 (Betriebsverfassungsgesetz). The shareholders' meeting is only bound by election proposals pursuant to §§ 6 and 8 of the Co-determination Act (Mitbestimmungsgesetz).

(2) A right to name members of the supervisory board may only be granted by the articles of association and only for specific shareholders or for the holder at the applicable time of specific shares. Holders of specific shares may only be granted the right to name supervisory board members if the shares are nominative shares (not bearer shares) and if their transfer requires the consent of the association. The shares of the holders of the right to name are not considered as a special class. Rights to name may only be granted for the maximum altogether of one third of the number of the members of the supervisory board as determined by the law or the articles of association. (*continues*)

§ 102

Term of office of the members of the supervisory board

(1) Members of the supervisory board may not be appointed for a period beyond the end of the shareholders' meeting which decides on the discharge from responsibility for the fourth fiscal year after the beginning of the term of office. The fiscal year in which the term of office begins is not counted.

(2) The office of the member for replacement terminates at the latest with the expiration of the term of office of the replaced member of the supervisory board.

§ 103**Removal of the members of the supervisory board**

(1) Members of the supervisory board who were elected by the shareholders' meeting without it being bound to an election proposal may be removed by it prior to the expiration of their term of office. The resolution requires a majority which comprises at least three fourths of the votes cast. The articles of association may determine a different majority and additional requirements.

(2) A member of the supervisory board who has been named to the supervisory board on the basis of the articles of association may be removed and replaced by another at any time by the party entitled to the right to name. If the preconditions for the right to name as determined by the articles of associations have ceased to exist, then the shareholders' meeting may remove the named member with a simple majority of votes.

(3) Upon motion by the supervisory board for cause regarding the person of a member of the supervisory board, the court shall remove this member. The supervisory board decides on making the motion with a simple majority. If the member of the supervisory board has been named to the supervisory on the basis of the articles of association, the the shareholders whose shares equal the aggregate of one tenth of the share capital or the nominal amount of two million Deutsche Mark may also make the motion. An immediate appeal is permissible against the decision.

(4) In addition to subsection 3, the Co-determination Act (Mitbestimmungsgesetz), the Co-determination Act concerning the coal and steel industry (Montan-Mitbestimmungsgesetz), Co-determination Amendment Act (Mitbestimmungsänderungsgesetz), and the Works Constitution Act 1952 apply to the removal of the members of the supervisory board who were neither elected by the shareholders' meeting without it being bound to an election proposal nor named to the supervisory board on the basis of the articles of association.

(5) The provisions for the removal of the member of the supervisory board apply to the removal of the member appointed for his replacement.

§ 111**Duties and rights of the supervisory board**

(1) The supervisory board shall supervise the management.

(2) The supervisory board may inspect and examine the books and records of the association as well as the assets, in particular the association's cash on hand and the inventory of securities and merchandies. It may also commission with this individual members or charge special experts with specific assignments.

(3) The supervisory board must call a shareholders' meeting if the welfare of the association requires it. For the resolution a simple majority suffices.

(4) Measures of the management cannot be conferred upon the supervisory board. The articles of association or the supervisory board may however determine that specific kinds of transactions may only be entered into with its consent. If the supervisory board refuses its consent, then the board of management may request that the shareholders' meeting decide on the consent. The resolution by which the shareholders' meeting consents requires a majority which comprises at least three fourths of the votes cast. The articles of association may determine neither a different majority nor additional requirements.

§ 116**Duty of diligence and liability of members of the supervisory board**

§ 93 regarding the duty of diligence and the liability of the members of the board of management apply accordingly to the duty of diligence and the liability of the members of the supervisory board.

§ 134**Voting right**

(1) The voting right is exercised pursuant to the nominal amounts of the shares. In case a shareholder owns several shares the articles of association may limit the voting right by determining a maximum amount or graduations. In addition the articles of association may determine that the shares which belong to another person for the account of a shareholder shall be counted together with the shares owned by the shareholder. In case the shareholder is an enterprise, it may in addition determine that, together with the shares owned by it, those shares which belong to an enterprise dependent on it or dominating it or being connected with it in a combine or which belong to another person for the account of such enterprises, shall also be counted. The limitations are not considered for the calculation of a capital majority required by the law or the articles of association.

(2) The voting right begins with the complete performance of the contribution. (*continues*)

(3) The voting right may be exercised by a holder of a proxy. It is required and sufficient that the proxy be in writing. The proxy shall be submitted to the association and remains in its custody.

(4) The form of exercising the voting right follows the articles of association.

§ 135**Exercising of the voting right by banks and persons acting professionally**

(1) A bank may only exercise or cause to be exercised a voting right for bearer shares which do not belong to it if it is authorized in writing. In its own shareholders' meeting the authorized bank may only exercise the voting right by virtue of the proxy to the extent that the shareholder has expressly given directives for the individual subjects on the agenda.

(2) A proxy may only be issued to a specific bank and only for the maximum of fifteen months. It is revocable at any time. The form of the proxy must be fully completed when it is issued and may not contain other declarations. It shall contain the date of the signing. The period in sentence 1 begins, at the latest, with the date of the signing.

(3) The authorized bank may only substitute persons who are not its employees if the proxy expressly permits a substitution and the authorized bank has no branch at the location of the shareholders' meeting. The same applies to a transfer of the proxy by the authorized bank.

(4) The bank may exercise the voting right from the proxy in the name and by naming the shareholder. If the proxy so determines the bank may also exercise the voting right in the name of whoever is concerned. If the bank exercises the voting right in the shareholder's name by naming him, the certificate of the proxy shall be submitted to the association and be held in custody by it. If it exercises the voting right in the name of whoever is concerned, the compliance with the requirements provided for in the articles of association for the exercise of the voting right is sufficient evidence towards the association of its right to vote; if the articles of association contain no provisions, the presentation of the shares or of a certificate to deposit of the shares with a notary or a securities deposit bank, suffices.

(5) If the shareholder has not given directives to the bank for exercising the voting right, then the bank shall exercise the voting right in accordance with its own proposals as communicated to the shareholders, pursuant to § 128 subsection 2, unless the bank may assume from the circumstances that the shareholder would, with the knowledge of the facts, approve of deviating in the exercise of the voting right.

(6) The effectiveness of the casting of the vote is not impaired by a violation of subsection 1 sentence 2, subsections 2, 3 and 5.

(7) A bank may exercise the voting right of nominative shares which do not belong to it and if it is entered into the stock ledger as their holder, only on the basis of a proxy in writing in the name and by naming the shareholder. Subsection 1 sentence 2, subsections 2, 3 and 5 shall apply to an authorization or to a proxy, in addition subsection 4 sentence 3 shall apply to the proxy. Otherwise subsection 6 applies.

(8) The bank shall inform the shareholder and give the reasons, if by exercising the voting right it has deviated from a directive of the shareholder or, if the shareholder has not given a directive, it has deviated from its own proposal as communicated to the shareholder pursuant to § 128 subsection 2.

(9) Subsections 1 to 8 apply accordingly to the exercising of the voting right by

1. associations of shareholders,
2. managers and employees of a bank, if the shares which do not belong to them have been entrusted to the bank for custody.
3. persons who professionally offer towards shareholders to exercise the voting right in the shareholders' meeting.

This does not apply if the person who wishes to exercise the voting right is the legal representative or the spouse of the shareholder or related to him up to the fourth degree of consanguinity or of relation by marriage.

(10) A bank is obligated to accept the order of a shareholder to exercise the voting right in a shareholders' meeting if it keeps shares of the association to exercise the voting right in the same shareholders' meeting. The obligation does not exist if the bank maintains no branch at the location of the shareholders' meeting and the shareholder has not permitted the transfer of the proxy to or the substitution of persons who are not employees of the bank.

(11) The liability of the bank to compensate for damages resulting from a violation of subsections 1 to 3, 5, 7, 8 or 10 may not be excluded nor limited in advance.

§ 291

Contract of domination. Contract to transfer profits

(1) Enterprise contracts are contracts by which a stock corporation or an association limited by shares subjects the direction of its association to another enterprise (contract of domination) or by which it obligates itself to transfer all its profits to another enterprise (contract to transfer profits). A contract by which a stock corporation or an association limited by shares undertakes to conduct its enterprise for the account of another enterprise is also considered as a contract to transfer all of the profit.

(2) If the enterprises which are not dependent on each other submit themselves by contract to a uniform direction, without having one of them become therewith dependent on another of the contracting enterprises, then this contract does not constitute a contract of domination.

§ 328**Limitation of rights**

(1) If a stock corporation or an association limited by shares and another enterprise constitute mutually participating enterprises, then as soon as the existence of the mutual participation has become known to one enterprise or the other enterprise has made a communication to it pursuant to § 20 subsection 3 or § 21 subsection 1, rights from the participations of the other enterprise which belong to it may only be exercised in the maximum of one fourth of the aggregate participation of the other enterprise. This does not apply to the right to new shares from a capital increase from reserves. § 16 subsection 4 is to be applied.

(2) the limitation of subsection 1 does not apply if before it had received such a communication from the other enterprise and before the existence of the mutual participation has become known to it, the enterprise has made a communication on its own to the other enterprise pursuant to § 20 subsection 3 or § 21 subsection 1.

(3) If a stock corporation or an association limited by shares and another enterprise constitute mutually participating enterprises, then the enterprises shall communicate to each other the amount of their participation and every change in writing without undue delay.

German Securities Trading Act 1995^{*}

§ 21

Duty to disclose

(1) Whoever reaches, exceeds or falls below by acquisition, sale or in any other way 5 per cent, 10 per cent, 25 per cent, 50 per cent, or 75 per cent of the voting rights in a stock-exchange listed stock corporation (party under a duty to report) shall notify the company and the Federal Supervisory Authority without delay in writing at the latest within 7 calendar days of the reaching, exceeding or falling below the specified thresholds as well as of the amount of his voting rights share and including his address. The notification period begins at the point in time at which the party under a duty to report has knowledge thereof or should have known according to the circumstances that his voting rights share has reached, exceeded or fallen below the specified thresholds.

(2) Companies listed on the stock exchange within the meaning of this Part are domestically domiciled companies whose stocks are admitted to official trading on a stock exchange in a member state of the European Communities or in another contracting state of the European Economic Area Agreement.

§ 22

Ascribing Voting Rights

(1) Voting rights arising from stocks of the stock exchange-listed company are deemed to be the equivalent of voting rights of the party under a duty to report for duties to report pursuant to § 21 subsection 1 if

1. the stocks belong to a third party and are kept by such third party for the account of the party under a duty to report or for the account of an enterprise controlled by the party under a duty to report,
2. the stocks belong to an enterprise which the party under a duty to notify controls,
3. the stocks belong to a third party with whom the party under a duty to notify or an enterprise controlled by it has concluded an agreement which binds both to pursue long-term joint purposes regarding management direction of the stock exchange-listed company in that they exercise their voting rights in unison,
4. the party under a duty to notify has assigned the stocks to a third party as collateral unless such third party is authorized to exercise the voting rights arising from such stocks and announces its intention to exercise such voting rights,
5. usufruct of the stocks has been granted to the benefit of the party under a duty to report,
6. the party under a duty to report or an enterprise controlled by it can acquire the stocks by unilateral declaration,
7. the stocks have been entrusted for safekeeping to the party under a duty to report and to

^{*} For a complete translation see *Peltzer/Scesniak*, German Securities Trading Act, Otto Schmidt Verlag, Köln, 1995. The translation provided here relies on this translation.

the extent that such party can exercise voting rights arising from such stocks in its own discretion if no special instructions of the stockholder are present.

(2) The voting rights to be ascribed are to be separately specified in the notifications pursuant to § 21 subsection 1 for each of the numbers in subsection 1.

(3) A controlled enterprise is an enterprise for which the party under a duty to notify, directly or indirectly,

1. has a right to the majority of the voting rights of the stockholders or of the shareholders,
2. has the right as stockholder or shareholder to appoint or recall the majority of the members of the administrative, directing or supervisory organ or
3. has exclusive rights as stockholder or shareholder to the majority of voting rights on the basis of an agreement concluded with other stockholders or shareholders of this enterprise.

§ 23

Non-consideration of voting rights

(1) The Federal Supervisory Authority shall permit, upon written request, that voting rights arising from stocks of the stock exchange-listed company shall not be considered in calculating the voting rights share if the applicant

1. is an enterprise admitted to participate in trading on a stock exchange in a member state of the European Communities or in another contracting state to the European Economic Area Agreement, which enterprise performs securities services,
2. holds or intends to hold the concerned stocks as trading stock and
3. indicates that the acquisition of the stocks is not intended to gain influence over the management direction of the company.

(2) The Federal Supervisory Authority shall permit, upon written request of an enterprise domiciled in a member state of the European Communities or in another contracting state to the European Economic Area Agreement and which enterprise does not meet the preconditions of subsection 1 no. 1 that voting rights from stocks of the stock exchange-listed company shall not be considered in respect of the 5 per cent notification threshold if the petitioner

1. holds or intends to hold the concerned stocks in order to make short-term use of existing or expected differences between the acquisition price and the sales price and
2. indicates that the acquisition of the stocks is not intended to exercise influence over the management direction of the company.

(3) In auditing the annual report of an enterprise which has been exempted pursuant to subsections 1 or 2, the annual report auditor shall determine in a separate memorandum whether the enterprise has followed the provisions of subsections 1 no. 2 or of subsection 1 no. 1 and shall submit such report together with the annual report audit to the legal representatives of the enterprise. The enterprise is obliged to submit such memorandum of the annual report auditor to the Federal Supervisory Authority without delay. The Federal Supervisory Authority can repeal the exemption pursuant to subsection 1 or 2 without consideration of the provisions of the Administrative Procedure Act (Verwaltungsverfahrensgesetz) if the duties pursuant to sentence 1 and 2 have not been met. If the exemption is rescinded or repealed, then the enterprise can apply anew for exemption at the earliest three years after the effective date of the rescission or repeal.

(4) Voting rights arising from stocks which shall not be considered because of an exemption pursuant to subsection 1 or 2 cannot be exercised if a duty to report pursuant to § 21 subsection 1 would exist in the event of their consideration.

§ 24

Notification by group companies

If a party under a duty to notify belongs to a group for which a group financial report must be produced pursuant to §§ 290, 340i of the Commercial Code, then the duties to report pursuant to § 21 subsection 1 can be performed by the parent company or, if the parent company is itself a subsidiary, by its parent company.

§ 25

Publication duties of the listed company

(1) The company listed on the stock exchange shall publicize reports pursuant to § 21 subsection 1 without delay, at the latest 9 calendar days after receipt of the report, in the German language in an official national stock exchange journal. The party under a duty to report is to be identified in the publication by name or firm name and residence or domicile. The company listed on the stock exchange shall announce in the Federal Gazette without delay the official stock exchange journal in which the report has been published.

(2) If the stocks of the stock exchange-listed company are admitted to official trading on a stock exchange in another member state of the European Communities or in another contracting state to the European Economic Area Agreement, then the company shall undertake publication pursuant to subsection 1 sentences 1 and 2 without delay, at the latest 9 calendar days after receipt of the report also in a stock exchange official journal of such country or, to the extent that the law of such country prescribes another form of informing the public, in such other form. The publication must be in a language which is permissible in such state for such publications.

(3) The stock exchange-listed company shall send the Federal Supervisory Authority proof of publication pursuant to subsections 1 and 2 without delay. The Federal Supervisory Authority shall inform such stock exchanges specified in subsection 2 of the publication.

(4) The Federal Supervisory Authority shall upon written application, exempt the stock exchange listed company from the duties to publicize pursuant to subsections 1 and 2 if the Authority is, after consideration of the circumstances, of the opinion that the publication would disserve the public interest or would inflict substantial damage upon the company to the extent, in the latter event, that non-publication could not lead to misleading of the public concerning assessment of the essential facts and circumstances of the concerned securities.

§ 26

Notification duties of companies domiciled abroad

(1) If the voting rights share of the stockholder of a foreign domiciled company whose stocks are admitted to official trading on a domestic stock exchange reach, exceed or fall below the thresholds specified in § 21 subsection 1 sentence 1, then the company is bound, to the extent that the preconditions of subsection 3 are not present, to publicize this fact and the extent of the voting rights share of the stock holder without delay, at the latest within 9 calendar days, in an official national stock exchange journal. The notice period begins at the point in time at which the company has knowledge that the voting rights share of the stockholder has reached, exceed or fallen below the thresholds specified in § 21 subsection 1 sentence 1.

(2) § 25 subsection 1 sentences 2 and 3, subsection 3 and 4 respectively shall be applied to publications pursuant to subsection 1.

(3) Companies domiciled in another member state of the European Communities or in another contracting state to the European Economic Area Agreement and whose stocks are admitted on a stock exchange to official trading must undertake publications prescribed by the law of the domiciliary state on the basis of Council Directive 88/627/EC of December 12, 1988, Article 10, concerning information to be publicized upon acquisition and sale of a substantial equity holding in a stock exchange-quoted company (O.J. L 348/62) domestically in a national stock exchange reporting journal in the German language. § 25 subsection 1 sentence 3 applies respectively.

§ 27

Evidence of reported equity holdings

Whoever has submitted a report pursuant to § 21 subsection 1 must, upon demand of the Federal Supervisory Authority or of the stock exchange-listed company prove the existence of the reported equity holding.

§ 28

Suspension of voting rights

Voting rights arising out of stocks belonging to a party under a duty to report or to an enterprise directly or indirectly controlled by such party may not be exercise for the time during which reporting duties pursuant to § 21 subsection 1 are not performed.

§ 29

Federal Supervisory Authority powers

(1) The Federal Supervisory Authority can demand information and the submission of documents of the stock exchange-listed company and of its stockholders to the extent that this is necessary to supervise the performance of the duties regulated in this Part. The powers pursuant to sentence 1 are in effect also in respect to persons and enterprises whose voting rights are to be ascribed pursuant to § 22 subsection 1. § 16 subsection 6 shall be applied.

(2) The Federal Supervisory Authority can issue guidelines according to which it decides in a normal case whether the preconditions for a reportable event under the duty to report or whether an exemption from the duties to report pursuant to § 21 subsection 1 are present. The guidelines shall be published in the Federal Gazette.

(3) The Federal Supervisory Authority can perform publications pursuant to § 25 subsections 1 and 2 at the cost of the stock-exchange listed company if the company does not perform its duty to publicize or performs such duty improperly, incompletely or not in the prescribed form.

§ 30

Cooperation with the relevant foreign authorities

(1) The Federal Supervisory Authority shall cooperate with the responsible offices of the other member states of the European Communities, of the other contracting states to the European Economic Area Agreement and, in the event of nos. 1 and 4, also with the appropriate authorities of third countries, in order especially to further that

1. parties under a duty to notify officially residing, domiciled or usually resident in one of these countries perform their duties to report in an orderly manner,
2. stock exchange-listed companies perform their duty to publicize pursuant to § 25 subsection 2 in an orderly manner,

3. the parties under a duty, pursuant to the regulations of another member state of the European Communities or of another contracting state to the European Economic Area Agreement, to notify in such country and with a domestic official residence, domestically domiciled or usually domestically residing perform their duties to report in an orderly manner,
4. foreign domiciled companies whose stocks are admitted to official trading on a domestic stock exchange perform their duties to publicize domestically in an orderly manner.

(2) The Federal Supervisory Authority may communicate facts, including information pertaining to specific individuals, to the responsible authorities of the other member states or contracting states to the extent that this is necessary to supervise observance of reporting and publication duties. In communicating facts, notice shall be given that the responsible authorities, without prejudice to their duties in criminal law matters concerning violations of reporting or publication duties, shall use the facts communicated to them (including information pertaining to specific individuals) exclusively to supervise observance of such duties or within the context of administrative or court proceedings in conjunction therewith.

(3) In the event of subsection 1 no. 3, the Federal Supervisory Authority enjoys powers pursuant to § 29 subsection 1.

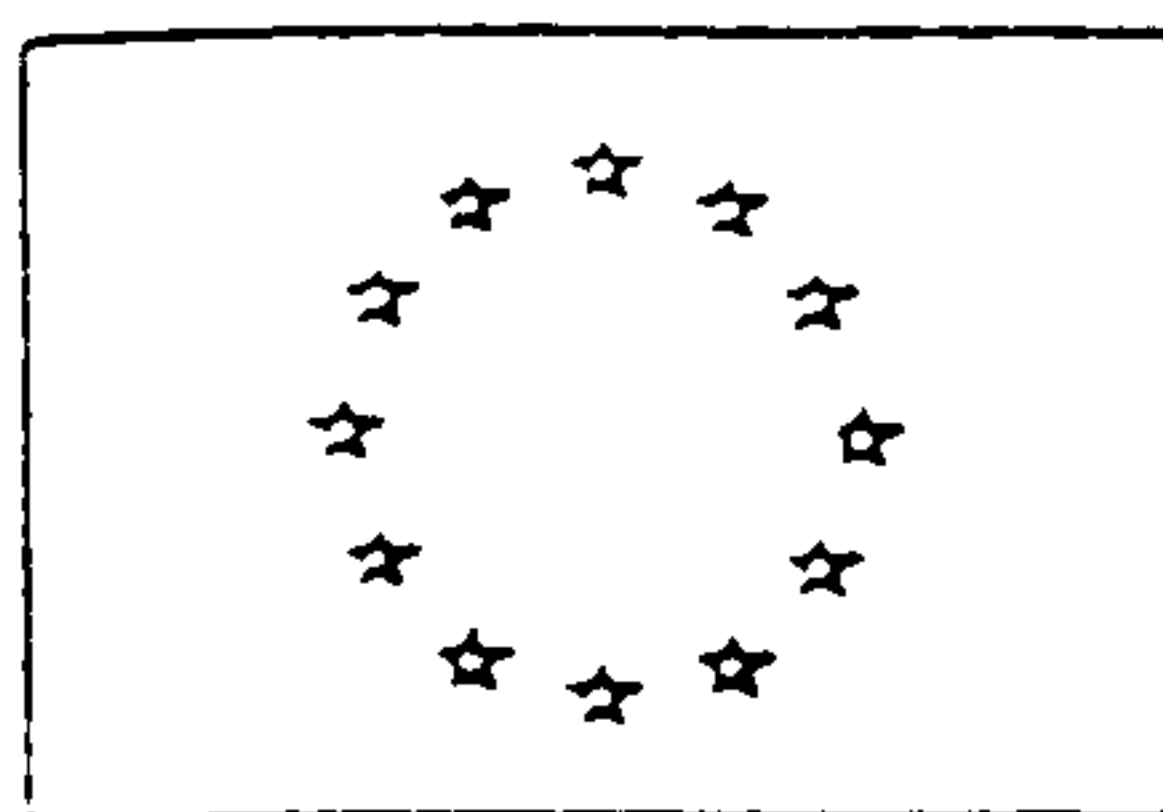
Bank Holdings 1995

Voting rights of the 10 largest German banks in listed German Stock Corporations as notified pursuant to § 21 of the Securities Trading Act

Bank	Holding	%
Bankgesellschaft Berlin AG	BHH Braunschweig-Hannoversche Hypothekenbank AG Hannover	60,0
	ASKO Deutsche Kaufhaus AG, Saarbrücken	10,5
Bayrische Hypotheken- und Wechselbank	Württembergischer Hypo Württembergische Hypothekenbank AG, Stuttgart	78,8
	Neue Baumwoll-Spinnerei und Weberei Hof AG, Hof	26,33
	AGROB AG, München	52,72
	Brau und Brunnen AG, Dortmund	33,38
	Allianz Aktiengesellschaft Holding München	5,0
	Rosenthal AG, Selb	15,0
Bayrische Landesbank Girozentrale	Bürgerliches Berghaus Ingolstadt AG, Ingolstadt	61,4
	Thüga AG, München	29,7
	Walter Bau-AG, Augsburg	16,9
	Süd-Chemie AG, München	18,96
Bayrische Vereinsbank AG	Vereins- und Westbank AG, Hamburg	75,0
	Neue Baumwoll-Spinnerei und Weberei Hof AG, Hof	42,4
	Süddeutsche Bodencreditbank AG, München	54,7
	Nürnberger Hypothekenbank AG, Nürnberg	85,4
	BHB Bayrische Handelsbank AG, München	76,4
	Aktien-Brauerei Kaufbeuren AG, Kaufbeuren	75,7
BFG Bank AG	Holzmann, Philipp AG, Frankfurt am Main	10,0
BHF-Bank Berliner Handels- und Frankfurter Bank	Deutsche Hypothekenbank (Actien-Gesellschaft), Hannover	75,1
	Wayss & Freytag AG, Frankfurt am Main	5,1
	AGIV Aktiengesellschaft für Industrie und Verkehrswesen, Frankfurt am Main	48,7

BW Bank Baden-Württembergische Bank AG	Württembergische AG, Versicherungs-Beteiligungsgesellschaft, Stuttgart	15,0
	Württembergische Lebensversicherung AG, Stuttgart	13,1
	ZEAG Zementwerk Lauffen Elektrizitätswerk Heilbronn AG, Heilbronn	6,25
Commerzbank Corporate Finance	RHEINHYP Rheinische Hypothekenbank AG, Frankfurt am Main	97,5
	Linde AG, Wiesbaden	10,2
	Salamander AG, Kornwestheim	10,7
	Karstadt AG, Essen	10,3
	PHOENIX AG, Hamburg	9,6
Delbruck & Co., Privatbankiers	Süd-Chemie Aktiengesellschaft, München	5,46
Deutsche Bank AG	Deutsche Beteiligungs AG Unternehmensbeteiligungsgesellschaft, Königstein	24,58
	Linde AG, Wiesbaden	10,1
	Daimler-Benz AG, Stuttgart	24,4
	Vögele, Joseph AG, Mannheim	9,95
	Holzmann, Philipp AG, Frankfurt am Main	25,83
	Frankfurter Hypothekenbank AG, Frankfurt am Main	94,32
	Deutsche Centralbodenkredit-AG, Berlin	95,24
	Hutschenreuther AG, Selb	25,1
	Schmalbach-Lubeca AG, Braunschweig	10,0
	Continental AG, Hannover	10,25
	Salamander AG, Kornwestheim	10,69
	Allianz AG Holding, München	10,0
	PHOENIX AG, Hamburg	10,0
	KHD Klöckner-Humboldt-Deutz AG, Köln	28,42
	Deutsche Bank Lübeck AG, vorm. Handelsbank Lübeck	93,78
DG Bank, Deutsche Genossenschaftsbank	BHF-Bank Berliner Handels- und Frankfurter Bank, Frankfurt am Main	9,61
	DVB Deutsche Verkehrs-Bank AG, Frankfurt am Main	55,41
	VK Mühlen AG, Hamburg	6,92
	AGAB AG für Anlagen und Beteiligungen, Frankfurt am Main	24,65

Dresdner Bank AG	Buderus AG, Wetzlar	11,1
	Deutsche Hypothekenbank Frankfurt AG, Frankfurt am Main	96,5
	HAMBURGHYP Hypothekenbank in Hamburg AG, Hamburg	86,2
	Continental Aktiengesellschaft, Hannover	6,5
	Münchener Rückversicherungs-Gesellschaft AG, München	9,9
	Bilfinger + Berger Bauaktiengesellschaft, Mannheim	25,1
	Allianz AG Holding, München	10,0
	OLB Oldenburgische Landesbank AG, Oldenburg	62,6
Frankfurter Bankgesellschaft gegr. 1899 AG	Binding Brauerei AG, Frankfurt am Main	36,04
GZB-Bank Genossenschaftliche Zentralbank AG	Württembergischer Hypo Württembergische Hypothekenbank AG, Stuttgart	10,0
Landesbank Schleswig- Holstein, Girozentrale	Jacobsen, W., AG, Kiel	59,03
Landwirtschaftliche Renten- bank, Frankfurt am Main	BM Bäckermühlen Aktiengesellschaft, Bietigheim-Bissingen	96,4
NORD LB Norddeutsche Landesbank Girozentrale	BHH Braunschweig Hannoversche Hypothekenbank AG, Hannover	30,0
	Bankgesellschaft Berlin AG, Berlin	15,01
	Continental AG, Hannover	17,9
Sal. Oppenheim jr. & Cie KGaA	Rheinboden Hypothekenbank AG, Köln	50,6
Schmidt Bank KGaA	Deutsche Beteiligungs AG Unternehmensbeteiligungsgesellschaft, Königstein	6,25
SüdwestLB, Südwestdeutsche Landesbank	Bürgerliches Brauhaus Ravensburg-Lindau AG, Ravensburg	15,83
Verband der Sparda-Banken e.V.	DVB Deutsche Verkehrs-Bank AG, Frankfurt am Main	15,6
Vereins- und Westbank AG	Geestemünder Bank AG, Bremerhaven	95,0
WestLB Westdeutsche Landesbank Girozentrale	Krupp, Friedr., AG Hoesch-Krupp, Essen	7,21
	Deutsche Babcock AG, Oberhausen	10,0
	Gerresheimer Glas AG, Düsseldorf	10,0
	Asko Deutsche Kaufhaus AG	10,5
	Stöhr & Co. AG, Mönchengladbach	19,48



COMMISSION OF THE EUROPEAN COMMUNITIES
 DIRECTORATE-GENERAL
 INTERNAL MARKET AND FINANCIAL SERVICES
 Company law and direct taxation
 Company law, industrial democracy and accounting standards

Brussels, 13.7.1993

XV/6019/93

XV.D.2 DIM/rb

Subject: Questionnaire on the regulation of take over bids

1. Many Member States have adopted legislation or codes of conduct in order to regulate changes in the control of companies listed on stock exchanges. However there are many differences between national regulations indicating that Member States do not pursue the same policy objectives or, even if that were the case, that their views differ concerning the need for and the effectiveness of various instruments which could be used to achieve these objectives.

The purpose of this questionnaire is to enable the Commission to assess the position of Member States on the following:

- the basic assumptions which are the heart of the Commission's proposal
- the measures proposed in order to meet the objectives of the proposal
- the present state of national legislations and the importance of takeovers in Member States' economies.

2. The Commission's modified proposal for a 13th Council directive, which met with strong resistance on the part of several Member States before Council meetings were discontinued in June 1991 was based on the following assumptions:

- a) There is a risk that shareholders suffer a reduction in the value of these shares if there is a change in control of their company

Do you agree

Yes/no

- b) Minority shareholders should be treated equally when a take over bid is made.

Do you agree

Yes/no

- c) Shareholders should be given sufficient time and information before they have to decide whether they accept a bid

Do you agree Yes/no

- d) The decision concerning a change in control should be made by the owners of the company and not by its management

Do you agree Yes/no

- e) The employees of the target company need to be informed as well.

Do you agree Yes/no

- f) Within the internal market the shareholders of listed public limited companies should be given equivalent guarantees.

Do you agree Yes/no

- g) Equivalent guarantees require a directive coordinating national measures

Do you agree Yes/no

3. Based on these assumptions the Commission had proposed the following main measures.

- a) - a right to exit for minority shareholders by way of a mandatory bid made by a new controlling shareholder and triggered by reaching a threshold (to cover 2 a)

Do you agree Yes/no

- b) - a procedure for voluntary or mandatory take over bids (for 100 % of remaining shares, equal conditions for all shareholders, full disclosure)
(to cover 2 b and 2 c)

Do you agree Yes/no

- c) - a restriction on defensive measures taken by management to frustrate bids without specific consultation of the shareholders' meeting (to cover 2 d)

Do you agree Yes/no

- d) - a right for employees to be fully informed by the bidder
(to cover 2 e)

Do you agree

Yes/no

4. Each of the measures listed under 3 could be covered

- a) at national level only, by law or self regulation
b) at Community level, by a directive or by recommendation
c) by a detailed directive or by a framework directive

DO YOU AGREE THAT THE FOLLOWING MEASURES ARE NEEDED AND SHOULD BE IMPOSED

	At national level		At Community level		
Content of measures	by law	by self regulation	by a detailed directive	by a framework directive	by a recommendation
Mandatory bid	yes/no	yes/no	yes/no	yes/no	yes/no
Equal treatment in case of any bid (mandatory and voluntary)	yes/no	yes/no	yes/no	yes/no	yes/no
Full disclosure to shareholders	yes/no	yes/no	yes/no	yes/no	yes/no
Full disclosure to workers	yes/no	yes/no	yes/no	yes/no	yes/no
limitation of defensive measures	yes/no	yes/no	yes/no	yes/no	yes/no

5. If you oppose a mandatory take over bid do you agree that there should be alternative measures giving equivalent protection

Yes/no

- a) If yes please describe briefly those alternative measures
b) If no please explain briefly why minority shareholders do not need special protection in the case of a change in control

6. If you are in favour of a mandatory bid do you agree that the bid should be triggered

- by crossing a threshold

Yes/no

- by the intention of crossing a threshold

Yes/no

- by the fact that shares had been acquired off the market at a higher price (control premium)

Yes/no

6 a) If you are in favour of a threshold do you agree that this threshold should not be higher than

- 51 %

Yes/no

- 33 %

Yes/no

- 25 %

Yes/no

6 b) If you are in favour of a threshold do you agree that there should be some derogations

Yes/no

7. If you are in favour of restricting the power of the target company's management to frustrate a take over bid do you agree that the management

- should not be allowed to take any frustrating measures

Yes/no

- should only be allowed to take measures approved by the shareholders' meeting once the bid has been declared

Yes/no

- should also be allowed to take measures authorised by the shareholders meeting within /12 months/ before a bid is declared

Yes/no

8. Has your takeover regulation been introduced or modified since the beginning of 1991

Yes/no

If yes please summarize new legislation

9. Do you have the intention to change your legislation

Yes/no

If yes please summarize intended changes

10. Please indicate the number of take over bids in your country in

		hostile	friendly
- 1990	Number		
- 1991	Number		
- 1992	Number		

P.S. The Commission will gladly receive any additional observations or comments you might wish to communicate to the Commission's services.

If you have any questions concerning the questionnaire please contact the secretariat of Mr. Wolff DG XV.D.2 (Tel: 295.4123 or Fax: 295.6500)

Proposal for a 13th European Parliament and Council Directive on Company Law Concerning Takeover Bids

- Brussels, 07.02.1996 - COM(95) 655 final -

The European Parliament and the Council of the European Union,

Having regard to the Treaty establishing the European Community, and in particular Article 54 thereof;

Having regard to the proposal from the Commission;

Having regard to the opinion of the Economic and Social Committee;

Whereas it is necessary to coordinate certain safeguards which Member States require of companies and firms within the meaning of the second paragraph of Article 58 of the Treaty for the protection of members and others, in order to make such safeguards equivalent throughout the Community;

Whereas it is necessary to protect the interests of shareholders of companies governed by the law of a Member State when these companies are subject to a takeover bid or to a change of control and their securities are admitted to trading on a regulated market within the scope of this Directive;

Whereas only action at Community level can ensure an adequate level of protection for shareholders throughout the Union and provide for minimum guidelines for the conduct of takeover bids; whereas Member States acting independently are not able to establish the same level of protection especially in the case of cross-border take-overs or purchases of control;

Whereas the adoption of a Directive is the appropriate procedure for laying down a framework consisting of certain common principles and a limited number of general requirements which Member States will be required to implement through more detailed rules according to their national systems and their cultural contexts;

Whereas Member States should take the necessary steps in order to protect shareholders having minority holdings after the purchase of the control of their company; whereas such a protection can be ensured either by obliging the person who acquired the control of a company to make a bid to all shareholders for all or for a substantial part of their holdings or by providing for other means which attain the objective of at least an equivalent level of protection of minority shareholders;

Whereas each Member State should designate an authority or authorities to supervise all aspects of the bid and to ensure that parties to takeover bids comply with the rules made pursuant to this Directive; whereas the different authorities must cooperate with one another;

Whereas it is desirable to encourage the voluntary control exercised by self regulatory bodies in

order to avoid recourse to administrative or judicial action;

Whereas to reduce the scope for insider dealing offerors should be required to announce their intention of launching a bid as soon as possible and to inform the supervisory authority and the offeree company's board of the bid before they are made public;

Whereas the addressees of a takeover bid should be properly informed of the terms of the bid by means of an offer document;

Whereas it is necessary to set a time limit for takeover bids;

Whereas to be able to perform their functions satisfactorily, supervisory authorities must at all times be able to require the parties to the bid to provide information on it;

Whereas to avoid operations which frustrate the bid it is necessary to limit the powers of the board of directors of the offeree company to engage in operations of an exceptional nature;

Whereas the board of the offeree company should be required to make public a document setting out its opinion on the bid and the reasons on which it is based;

Whereas it is necessary that Member States provide for rules covering the cases when the bid may be withdrawn or declared void once the offer document has been made public, the right of the offeror to revise its bid, the possibility of competing bids for the securities of a company which are necessary to the advantage of its shareholders and the disclosure of the result of the bid;

have adopted this Directive

Article 1: Scope

The coordination measures prescribed by this Directive shall apply to the laws, regulations and administrative provisions or other mechanisms or arrangements of the Member States relating to takeover bids for the securities of a company governed by the law of a Member State, where such securities are admitted, wholly or partially, to trading on a market in one or more Member States which is regulated and supervised by authorities recognised by public bodies, operates regularly and is accessible, directly or indirectly, to the public.

Article 2: Definitions

For the purposes of this Directive:

- "takeover bid" ("bid") shall mean an offer made to the holders of the securities of a company to acquire all or part of such securities by payment in cash and/or in exchange for other securities. A bid may be either mandatory, if so provided by Member States as means to protect minority shareholders, or voluntary;
- "offeree company" shall mean a company whose securities are the subject of a bid;
- "offeror" shall mean any natural person or legal entity in public or private law making a bid;

- "securities" shall mean transferable securities carrying voting rights in a company or conferring entitlement to obtain transfereable securities carrying such rights;
- "parties to the bid" shall mean the offeror, the members of the offeror's administrative or management board, if the offeror is a company, the addressees of the bid and the members of the administrative or management board of the offeree company.

Article 3: Protection of minority shareholders

1. Where a natural person or legal entity who as a result of acquisition, holds securities which added to any existing holdings give him a specified percentage of voting rights in a company referred to in Article 1, conferring on him the control of that company, Member States should ensure that rules or other mechanisms or arrangements are in force which either oblige this person to make a bid in accordance with article 10 or offer other appropriate and at least equivalent means in order to protect the minority shareholders of that company.
2. The percentage of voting rights which confers control for the purposes of paragraph 1 and the way of its calculation shall be determined by the law of the Member State where the supervisory authority is located.

Article 4: Supervisory authority

1. Member States shall designate the authority or authorities, which will supervise all aspects of the bid. The authorities thus designated may include associations or private bodies. Member States shall inform the Commission of these designations and shall specify all divisions of functions that may be made.
2. the authority competent for supervising the bid shall be that of the Member State in which the offeree company has its registered office if the securities of the company are admitted to trading on a regulated market in that Member State. Otherwise, the competent authority shall be that of the Member State on whose regulated market the securities of the company were first admitted to trading and are still traded.
3. Without prejudice to their duty of professional secrecy, the competent authorities of the Member States shall cooperate, in so far as necessary for the performance of their duties and for this purpose shall supply each other with any information that may be necessary.
4. The supervisory authorities shall have all the powers necessary for the exercise of their functions, which shall include responsibility for ensuring that the parties to a bid comply with the rules made pursuant to this Directive. In addition Member States can provide that their supervisory authorities may, on the basis of a reasoned decision, grant derogations from the rules drawn up in accordance with this Directive provided that in granting such derogations the supervisory authorities shall respect the principles mentioned in article 5.
5. This Directive does not affect the power which courts may have in a Member State to decline to hear legal proceedings and to decide whether or not such proceedings affect the outcome of the bid provided that an injured party enjoys adequate remedies, whether through an appeals

procedure operated by the supervisory authority or through the right to take proceedings before the courts to claim compensation.

Article 5: General principles

1. For the purposes of the implementation of this Directive, Member States shall ensure that the rules or other arrangements made pursuant to this Directive respect the following principles:

- (a) all holders of securities of an offeree company who are in the same position are to be treated equally;
- (b) the addressees of a bid are to have sufficient time and information to enable them to reach a properly informed decision on the bid;
- (c) The board of an offeree company is to act in the interests of the company as a whole;
- (d) false markets must not be created in the securities of the offeree company, of the offeror company, or of any other company concerned by the bid;
- (e) offeree companies must not be hindered in the conduct of their affairs for longer than is reasonable by a bid for their securities.

2. In order to attain the objective set out in paragraph 1, Member States shall ensure that rules are in force which satisfy the minimum requirements set out in the following articles.

Article 6: Information

1. Member States shall ensure that rules are in force requiring that the decision to make a bid is made public and that the supervisory authority and the board of the offeree company are informed of the bid before this decision is made public.

2. Member States shall ensure that rules are in force requiring the offeror to draw up and make public in good time an offer document containing the information necessary to enable the addressees of the bid to reach a properly informed decision on the bid. Before the offer document is made public, the offeror shall communicate it to the supervisory authority.

3. Those rules shall require that the document state at least:

- the terms of the bid;
- the identity of the offeror or, where the offeror is a company, the type, name and registered office of that company;
- the securities or class or classes of securities for which the bid is made;
- the consideration offered for each security or class of securities and the basis of the valuation used in determining it with particulars of the way in which the consideration is to be given;
- the maximum and minimum percentages or quantities of securities which the offeror undertakes to acquire;

- details of any existing holdings of the offeror in the offeree company;
- all conditions to which the offer is subject;
- the offeror's intentions with regard to the future business and undertakings of the offeree company; its employees and its management;
- the period for acceptance of the bid, which may not be less than four weeks or more than ten weeks from the date on which the document is made public;
- where the consideration offered by the offeror includes securities, information abouts those securties.

4. Member States shall ensure that rules are in force requiring that the parties to a bid to provide the supervisory authority at any time on request with all information in their possession concerning the bid which the supervisory authority considers necessary for the discharge of its functions.

Article 7: Disclosure

1. Member States shall ensure that rules are in force which require a bid to be made public in such a way as to avoid the creation of false markets in the securities of the offeree company or of the offeror.

2. Member States shall ensure that rules are in force which provide for the disclosure of all information or documents required in such a manner as to ensure that they are both readily and promptly available to the addressees of the bid.

Article 8: Obligations of the board of the offeree company

Member States shall ensure that rules are in force requiring that:

- a) after receiving the information concerning the bid and until the result of the bid is made public, the board of the offeree company should abstain from any action which may result in the frustation of the offer, and notably from the issuing of shares which may result in a lasting impediment ot the offeror to obtain control over the offeree company, unless it has the prior authorisation of the general meeting of the shareholders given for this purpose;
- b) the board of the offeree company shall draw up and make public a document setting out its opinion on the bid together with the reasons on which it is based.

Article 9: Rules applicable to the conduct of bids

In addition Member States shall ensure that rules are in force which govern the conduct of bids at least for the following matters:

- a) withdrawal or nullity of the bid
- b) revision of bids
- c) competing bids
- d) disclosure of the result of bids

Article 10: Mandatory bid

1. Where a Member State provides for a mandatory bid as a means to protect the minority shareholders, this bid shall be launched to all shareholders for all or for a substantial part of their holdings at a price which meets the objective of protecting their interests.
2. If the mandatory bid comprises only a part of the securities of the offeree company and shareholders offer to sell to the offeror more shares than the partial offer covers, shareholders should be treated equally by means of a pro rata treatment of their shareholdings.

Article 11: Transposition of the Directive

1. Member States shall ensure that the laws, regulations and administrative provisions or other mechanisms or arrangements necessary for them to comply with this Directive are in force before 1 April 1998.
2. Member States shall communicate to the Commission the provisions or other arrangements referred to in paragraph 1, making express reference to this Directive.

Article 12: Addressees of the Directive

This Directive is addressed to the Member States.

Merger Control Provision of the German Act Against Restraints of Competition

- Gesetz gegen Wettbewerbsbeschränkungen vom 20. Februar 1990 -

Part Three Market-Dominating Enterprises

§ 22

Market Domination; Presumptions; Abuse Control

(1) An enterprise is market dominating within the meaning of this Act if it, either as one offering or calling for a specific kind of goods or commercial services,

1. is without competitors or is subject to no substantial competition; or
2. has a paramount market position in relation to its competitors; in this context, in addition to its market share, regard shall be given in particular to its financial strength, its access to the supply and sales markets, its inter-relationships with other enterprises as well as to legal or factual barriers to the entry of other enterprises into the market, the ability to shift its supply or demand to other goods or commercial services, as well as the possibility of the opposite market side to change to other enterprises.

(2) Furthermore, two or more enterprises shall be deemed to be market dominating insofar as, for factual reasons, substantial competition between them for a specific kind of goods or commercial services does not exist, either generally or in specific markets, and insofar as they in their entirety fulfill the conditions of subsection (1).

(3) It shall be presumed that

1. an enterprise is market dominating within the meaning of subsection (1) if it has a market share of at least one-third for a specific kind of goods or commercial services; this presumption shall not apply if the turnover proceeds of the enterprise during the last preceding business year amounted to less than 250 million Deutsche Marks;
2. the conditions specified in subsection (2) are fulfilled if, with respect to a specific kind of goods or commercial services,
 - a) three or fewer enterprises together have a market share of 50 per cent or more, or
 - b) five or fewer enterprises together have a market share of two-thirds or more;

this presumption shall not apply insofar as enterprises are concerned whose turnover proceeds during the last preceding business year amounted to less than 100 million Deutsche Marks. § 23 (1), sentences 2 to 10, shall apply analogously to the calculation of market shares and turnover proceeds.

(4) In respect of market dominating enterprises, the Cartel Authority shall have the powers set out in subsection (5), insofar as such enterprises abusively exploit their market dominating position in the market for these or other goods or commercial services. An abuse within the meaning of sentence 1 shall exist in particular if a market dominating enterprise as one offering or calling for a specific kind of goods or commercial services

1. impairs, without justifiable cause in a way materially affecting competition in the market, the opportunities of other enterprises to compete;
2. demands prices or other business terms deviating from those which would have been agreed on with a high degree of likelihood if effective competition had existed; in this

context, particular regard shall be given to the conduct of other enterprises active on comparable markets on which effective competition exists;

3. demands less favourable prices or other business terms than those demanded by the market dominating enterprise itself on comparable markets from purchasers of the same kind, unless there is a justifiable cause for the difference made.

(5) Under the conditions of subsection (4), the Cartel Authority may prohibit abusive conduct of market dominating enterprises and declare agreements to be ineffective; § 19 shall apply analogously. Prior to such action, the Cartel Authority should call upon the parties involved to cease and refrain from the abuse objected to.

(6) Insofar as the conditions of subsection (1) are fulfilled by group enterprise within the meaning of § 18 Stock Corporations Act, the Cartel Authority shall have the powers pursuant to subsection (5) with respect to each enterprise of the group.

§ 23

Report of Mergers

(1) A merger of enterprises shall be reported to the Federal Cartel office without undue delay if in the last business year preceding the merger, the participating enterprises had collectively turnover proceeds of not less than 500 million Deutsche Marks. If a participating enterprise constitutes a dependent or dominating enterprise within the meaning of § 17 of the Stock Corporation Act or a group enterprise within the meaning of § 18 of the Stock Corporation Act then the enterprises so connected shall be regarded as a single enterprise for purposes of computing turnover proceeds and market shares; if several enterprises, on the basis of an agreement or otherwise, act together in such a manner that they can jointly exercise a dominating influence over a participating enterprise, then each of them shall be deemed to be a dominating enterprise. § 277 (1) of the Commercial Code shall apply to the calculation of turnover proceeds; turnover proceeds from sales and services between enterprises which are connected within the meaning of sentence 2 (internal turnover proceeds) and consumption taxes shall not be taken into account; turnover proceeds in foreign currencies shall be converted into Deutsche Marks at the official exchange rate. In respect of banks and building loan savings banks, one-tenth of total sales, and in respect of insurance companies, the premium income of the last preceding business year, shall be substituted in place of turnover proceeds. The amount of total assets shall be reduced by those items which reflect participations in connected enterprises within the meaning of sentence 2; premium income shall be the income derived from the prime- and re-insurance business, including the part thereof expended for re-insurance. For enterprises whose business consists in whole or in part of distribution of goods, only three-fourths of the turnover proceeds therefrom shall be taken into account. For enterprises whose business consists in whole or in part in the publication, production or distribution of newspapers or periodicals or parts thereof, twenty times the turnover proceeds shall be taken into account; sentence 6 shall remain unaffected. In the case of an acquisition of the assets of another enterprise in whole or in substantial part, the computation of market shares and turnover proceeds of the seller shall be based only on the part of the assets sold. Sentence 8 shall apply analogously to the acquisition of shares, insofar as less than 25 per cent of the shares remain with the seller and the merger does not fulfill the prerequisites of subsection (2), No. 2, sentence 3, Nos. 5 or 6. A person or an association of persons, neither of which is an enterprise, shall be deemed to be an enterprise for the purposes of this Act, if such person or association holds a majority interest in another enterprise.

(2) The following transactions shall be deemed to be a merger within the meaning of this Act:

1. The acquisition of the assets of another enterprise in whole or in substantial part by amalgamation, consolidation, short merger or other means.
2. The acquisition of shares in another enterprise, if such shares alone or together with other shares already held by the enterprise
 - a) equal or exceed 25 per cent of the capital or the voting rights of the other enterprise; or
 - b) equal or exceed 50 per cent of the capital or the voting rights of the other enterprise, or

c) secure the enterprise a majority interest within the meaning of § 16 (1) of the Stock Corporation Act.

The shares held by the enterprise are deemed to include also those shares which are held either by a connected enterprise within the meaning of subsection (1), sentence 2, or by another for the account of these enterprises and, where the owner of the enterprise is a sole proprietor, also those shares which form part of other assets of the owner. If several enterprises acquire within the above-described scope, simultaneously or successively, shares of another enterprise, this shall also be deemed to be a merger among the participating enterprises with regard to those markets in which such other enterprise is active (joint venture). Furthermore, the acquisition of shares shall also be deemed to be a merger, insofar as the purchaser is afforded by agreement, articles of association or resolution a legal position equivalent to that of a shareholder in a stock corporation holding more than 25 per cent of the voting capital.

3. Agreements with another enterprise by means of which
 - a) an enterprise group within the meaning of § 18 of the Stock Corporation Act is created, or the number of group enterprises is enlarged; or
 - b) such other enterprise obligates itself to conduct its business for the account of the enterprise or to transfer its profits in whole or in part to the enterprise; or
 - c) the business of the other enterprise is leased or otherwise transferred in whole or in part to the enterprise.
4. The placing of the same persons, to the extent of at least one-half of the members thereof, on the supervisory board, on the board of management, or on such other corporate organ as may be authorized to conduct the management of enterprises.
5. Any other combination of enterprises on the basis of which one or several enterprises can exercise directly or indirectly a dominating influence on another enterprise.
6. Any combination of enterprises as designated in Nos. 2, 4, or 5 in connection with which shares of a lesser amount than specified in No. 2, sentence 1, subpara. a), are acquired, a legal position pursuant to No. 2, sentence 4, is not afforded, the scope of identity of persons required by No. 4 is not achieved, or the exercise of a dominant influence within the meaning of No. 5 is not possible, provided that as a result of the combination one or several enterprises can exercise directly or indirectly an influence on another enterprise that is material with regard to competition.

(3) A merger is presumed to exist also if the participating enterprises have previously been merged within the meaning of subsection (2), unless the merger does not lead to a substantial strengthening of the already-existing enterprise connection. It does not constitute a merger if a bank, in connection with the formation or capital increase of an enterprise or otherwise in the course of its business, acquires shares of another enterprise for the purpose of selling such shares in the market, provided that it does not exercise voting rights arising from such shares, and provided that the sale is made within one year; in connection with the formation of an enterprise, the exercise of voting rights in the first shareholders' meeting after the formation does not constitute a merger. If an enterprise participating in a merger constitutes a connected enterprise within the meaning of subsection (1), sentence 2, then the dominating enterprise as well as those enterprises on which the dominating enterprise is dependent shall be deemed to be a participating in the merger. If two or more enterprises merge, this shall also be deemed to be a merger of their dependent enterprises.

(4) The following shall be obligated to make the report:

1. in the cases of an amalgamation, consolidation or short merger, the owners of the transferee enterprises or the newly-formed enterprise or their representatives, and, in the case of legal entities or partnerships, those persons who, by law or articles of association, are authorized to act as representatives,
2. otherwise
 - a) the owners of the enterprises participating in the merger; and
 - b) in the case of subsection (2), Nos. 1 and 2, also the seller or their representatives, and

in the case of legal entities or partnerships, those persons who, by law or articles of association, are authorized to act as representatives; in the case of lit. b), subsection (3), sentence 3, shall apply analogously.

(5) The form of the merger shall be indicated in the report. The report shall further contain the following information regarding each participating enterprise:

1. name or other designation and place of business or legal residence,
2. type of business,
3. the market shares, including the basis for their computation or estimation, if for the participating enterprises together such market shares amount to at least 20 per cent within the territory in which this Act applies or within a substantial part thereof, and the turnover proceeds; in the case of insurance companies, the premium income shall substitute the turnover proceeds;
4. when shares of another enterprise are acquired, the amount of the shares acquired and of the aggregate participation held.

If a participating enterprise is a connected enterprise within the meaning of subsection (1), sentence 2, then the information required pursuant to sentence 2, Nos. 1 and 2, shall also be given with respect to the enterprises so connected and the information required pursuant to sentence 2, No. 3, shall be given for each enterprise participating in the merger and together for the enterprises so connected with it, and the group relationships and the dependancy and participation relationships among the connected enterprises shall be reported.

(6) The Federal Cartel Office may demand from each participating enterprise information regarding market shares, including the basis for their calculation or estimation, and regarding turnover proceeds for a specific kind of goods or commercial services, which have been realized by the enterprise in the last business year preceding the merger. If a participating enterprise constitutes a connected enterprise within the meaning of subsection (1), sentence 2, then the Federal Cartel Office may also demand information regarding the enterprises so connected; it may demand information also from the connected enterprises. § 46 (2), (5), and (9) shall apply analogously. The Federal Cartel Office shall determine a reasonable period for the furnishing of such information. The powers of the Federal Cartel Office pursuant to § 46 shall remain unaffected.

§ 23a

Presumptions

(1) § 22 (1) to (3) notwithstanding, for purposes of merger control it shall be presumed that a merger will create or strengthen a paramount market position if

1. an enterprise which had during the last business year preceding the merger turnover proceeds of at least two thousand million Deutsche Marks mergers with another enterprise which
 - a) is active in a market in which small and medium-sized enterprises collectively have a market share of at least two-thirds and the enterprise participating in the merger together have a market share of at least five percent; or
 - b) has a market dominating position in one or several markets in which an aggregate turnover of at least one hundred and fifty million Deutsche Marks was achieved during the last preceding calendar year; or
2. the enterprises participating in the merger had collectively during the last business year preceding the merger turnover proceeds of at least twelve thousand million Deutsche Marks and at least two of the enterprises participating in the merger individually had turnover proceeds of at least one thousand Deutsche Marks; this presumption shall not apply insofar as the merger fulfills also the requirements of § 23 (2), No. 2, sentence 3, and the joint venture is not active in a market in which a turnover of at least seven hundred and fifty million Deutsche Marks was achieved during the last preceding calendar year.

(2) For purposes of merger control an entirety of enterprises shall be deemed to be market dominating if they consist of

1. three or fewer enterprises which have in market the highest market shares and together a market share of 50 per cent; or
2. five or fewer enterprises which have in a market the highest market shares and together a market share of two-thirds,

unless the enterprises demonstrate that the competitive situation permits the expectation that substantial competition between them will remain in existence after the merger or such entirety of enterprises does not have a superior market position in relation to the other competitors. Sentence 1 shall not apply insofar as enterprises are concerned which had turnover proceeds of less than one hundred and fifty million Deutsche Marks during the last preceding business year or if the enterprises participating in the merger collectively had a market share of less than 15 per cent. § 22 (2) and (3), sentence 1, No. 2, shall remain unaffected.

(3) § 23 (1), sentences 2 to 6 and 8 to 10 apply analogously to the calculation of turnover proceeds and market shares.

§ 24

Control of Mergers

(1) If it is to be expected that a merger will create or strengthen a market dominating position, the Cartel Authority shall have the powers set forth in the following provisions, unless the participating enterprises demonstrate that, by means the merger, improvements of the competitive conditions will also occur and that these improvements will outweigh the disadvantages of the market domination.

(2) If the conditions of subsection (1) are met, the Federal Cartel Office must prohibit the merger. The Federal Cartel Office may prohibit a merger as soon as the plan for the merger has become known to it; the Federal Cartel Office may prohibit completed mergers only within one year after receipt of the complete report pursuant to § 23; § 24a (2), sentence 2, Nos. 1 and 5 to 6, shall apply analogously. Prior to such prohibition, the highest authorities of the states in which the participating enterprises maintain their legal residence shall be given the opportunity for comment. If the Federal Cartel Office has issued the order pursuant to sentence 1, it shall be unlawful to consummate the merger without permission of the Federal Minister of Economics or to participate in its consummation; legal transactions in violation of this prohibition shall be invalid; this provision shall not apply to agreements concerning an amalgamation, consolidation, short merger, integration or formation of an enterprise nor to enterprise agreements within the meaning of §§ 291 and 292 of the Stock Corporation Act, when such agreements have become legally effective by entry in the Commercial Register or the Register of Cooperatives. A completed merger which has been prohibited by the Federal Cartel Office shall be dissolved, unless the Federal Minister of Economics grants permission for the merger.

(3) The Federal Minister of Economics shall, on application, grant permission for the merger, if in the individual case the restraint of competition is compensated by the overall economic advantages of the merger or if the merger is justified by an overriding public interest; in this connection, regard shall also be given to the competitive capability of the participating enterprises in the markets outside the territory in which this Act applies. The permission may only be granted if the scope of the restraint of competition does not endanger the principle of the market economy. The permission may be subjected to restrictions and duties. These may not be directed at placing the conduct of the participating enterprises under continuous supervision. § 22 shall remain unaffected.

(4) The application for the granting of permission for the merger shall be submitted to the Federal Minister of Economics in writing within a period of one month. The period shall commence with the service of the order of the Federal Cartel Office referred to in subsection (2), sentence 1; if the order of the Federal Cartel Office is appealed within the period provided for in § 65 (1), sentences 1 and 2, then the period for the application for permission shall commence on the date on which the order of the Federal Cartel Office becomes unappealable. The Federal Minister of Economics should decide on the application within four months following the

expiration of the periods for the application for permission referred to in sentences 1 and 2. Prior to the ministerial decision, the highest authorities of the states in which the participating enterprises maintain their legal residence shall be given opportunity for comment.

(5) The Federal Minister of Economics may revoke the premission, amend it by ordering restrictions or subject it to duties, if the participating enterprises contravene a duty connected with the permission. The Federal Minister of Economics may withdraw the permission if the participating enterprises have obtained it through fraud, threat, bribery or through furnishing of information incorrect or incomplete in material aspects.

(6) The dissolution of a completed merger may also be accomplished by removing the restraint of competition in a manner other than through the re-establishment of the originally prevailing conditions. The Federal Cartel Office shall order the measures necessary for the dissolution of the merger if

1. its order referred to in subsection (2), sentence 1, has become unappealable; and
2. in case the participating enterprises had filed an application for the granting of permission with the Federal Minister of Economics, the rejection of such application, or, in the case of subsection (5), the revocation or withdrawal have become unappealable.

In this connection, the Federal Cartel Office, with due regard for the preservation of the interests of third parties, shall order those measures which accomplish the objective with the least expense and the least burden for those involved.

(7) The Federal Cartel Office may, for purposes of enforcing its order, in particular

1. compel those who are obligated to dissolve the merger to carry out the ordered measures without undue delay by imposing one or more times an enforcement fine between 10.000 and one million Deutsche Marks;
2. prohibit the exercise of voting rights attached to shares of a participating enterprise which are held by or to by attributed to another participating enterprise, or subject the exercise of such voting rights or the manner of such exercise to permission of the Federal Cartel Office;
3. declare agreements effecting mergers as designated in § 23 (2), Nos. 1 and 3, to be ineffective; this provision shall not apply to agreements concerning an amalgamation, consolidation, short merger, integration or formation of an enterprise nor to enterprise agreements within the meaning of §§ 291 and 292 of the Stock Corporation Act, when such agreements have become legally effective by entry in the Commercial Register or in the Register of Cooperatives;
4. appoint a fiduciary who shall make the required legal declarations and carry out the required acts on behalf of the parties obligated to dissolve the merger; in this connection, the extent to which the rights of those concerned shall be suspended during the duration of the fiduciary relationship shall be specified; §§ 664 and 666 to 670 of the Civil Code shall be applied analogously to the legal relation between the fiduciary and such obligated parties; the fiduciary may claim a reasonable compensation from such obligated parties.

(8) Subsections (1) to (7) shall not apply

1. if the aggregate turnover proceeds of the participating enterprises collectively amounted to less than five hundred million Deutsche Marks during the last preceding business year; or
2. if an enterprise which is not a dependent enterprise and which had during the last preceding business year turnover proceeds of not more than 50 million Deutsche Marks joins another enterprise, unless the enterprise had turnover proceeds of at least four million Deutsche Marks and the other enterprise had turnover proceeds of at least on thousand million Deutsche Marks, or
3. insofar as a market is concerned in which goods or commercial services are offered for at least five years and in which a turnover of less than ten million Deutsche Marks was achieved during the last calender year.

§ 23 (1), sentences 2 to 10, shall be applied in computing turnover proceeds.

(9) Subsection (8), sentence 1, No. 2, shall not be applied insofar as by reason of the merger

competition is restricted within the meaning of subsection (1) in respect of the publication, production, or distribution of newspapers or periodicals or of parts thereof.

§ 24a

Notification of Merger Plans

(1) Notification of the plan for a merger may be given to the Federal Cartel Office. Notification of the merger plan must be given to the Federal Cartel Office if

1. one of the enterprises participating in the merger had turnover proceeds of at least two thousand million Deutsche Marks during the last preceding business year; or
2. at least two of the enterprises participating in the merger had each turnover proceeds of one thousand million Deutsche Marks or more during the last preceding business year; or
3. if the merger, pursuant to state law, is to be effected by legislative enactment or by any other sovereign act;

this provision shall not apply to mergers pursuant to § 23 (2), No. 6. § 23 shall apply analogously to the notification, provided that in the application of § 23 (1), sentence 1, and § 23 (6), the date of the notification shall be substituted for the date of the merger, and provided further, that in cases of an amalgamation, consolidation or short merger the owners, representatives or persons authorized to represent the enterprises participating in the merger shall be required to give the notification. The notification shall only be deemed to be effected if it contains the particulars referred to in § 23 (5). § 46 (9) shall apply analogously to the knowledge and documents obtained on the occasion of the notification.

(2) If notification of the merger plan has been given to the Federal Cartel Office, the Federal Cartel Office may prohibit the merger only if it informs whoever has given the notification that it has begun an examination of the merger plan issues the order pursuant to § 24 (2), sentence 1, within four months after receipt of the notification. However, the Federal Cartel Office may prohibit the merger after the expiration of the four-months period if

1. the enterprises participating in the merger have agreed to an extension of the period; or
2. the merger is completed even though the one-month period referred to in sentence 1, the four-month period therein referred to has not yet expired; or
3. the merger is completed in a manner other than as notified; or
4. the merger has not yet been completed and the circumstances, on the basis of which the Federal Cartel Office has refrained from giving information pursuant to sentence 1 or from prohibiting the merger pursuant to § 24 (2), sentence 1, have materially changed; or
5. the Federal Cartel Office has been caused, by incorrect or incomplete information given by the enterprises participating in the merger or by another, to abstain from giving information pursuant to sentence 1 or from prohibiting the merger pursuant to § 24 (2), sentence 1; or
6. a demand for information pursuant to §§ 23 (6) or 46 was not, or not in time, fulfilled thereby causing the conduct of the Federal Cartel Office referred to in No. 5.

(3) The notification of the merger plan shall not affect the obligation to report the merger pursuant to § 23; in the report pursuant to § 23, reference may be made to the documents submitted with the notification of the merger plan.

(4) If notification of a merger plan must be given pursuant to subsection (1), sentence 2, it shall be unlawful either to complete the merger or to participate in the completion of the merger prior to the expiration of the one-month period referred to in subsection (2), sentence 1, and, in case the Federal Cartel Office has given information pursuant to subsection (2), sentence 1, prior to the four-months period therein referred to or its consented-to extension, unless the Federal Cartel Office has informed the notifying party in writing prior to the expiration of the periods referred to in subsection (2), sentence 1, that the merger plan does not fall under the prohibition requirements of § 24 (1); legal transactions in violation of this prohibition shall be invalid; this provision shall not apply to agreements concerning an amalgamation, consolidation,

short merger, integration or formation of an enterprise nor to enterprise agreements within the meaning of §§ 291 and 292 of the Stock Corporation Act, when such agreements have become legally effective by entry in the Commercial Register or in the Register of Cooperatives.

§ 24b

Monopolies Commission

(1) A Monopolies Commission shall be established to regularly give its opinion on the development of enterprise concentration in the Federal Republic of Germany and on the administration of §§ 22 to 24a. It shall be composed of five members who must have particular knowledge and experience in the fields of economics, business administration, social policy, technology or business law.

(2) The members of the Monopolies Commission may belong neither to the Government nor to the legislature of the Federation or a state, nor to the civil service of the Federation, a state or any other legal entity under public law, with the exception of university professors and members of an academic institute. Furthermore, they may not be representatives of a business association nor of an organization of employers or employees, nor have a permanent employment or other permanent service contract with such association or organization. Furthermore, they may not have held such a position during the year preceding appointment as a member of the Monopolies Commission.

(3) In its opinion, the Monopolies Commission should evaluate the prevailing state of enterprise concentration as well as its foreseeable development in the light of economic policy, in particular competition policy, and appraise the administration of §§ 22 to 24a. It should also indicate amendments of the pertinent provisions of this Act which it deems to be necessary.

(4) The Monopolies Commission shall only be bound by the mandate established by this Act and shall be independent in its activities. If a minority is of a dissenting view in the preparation of the opinions, then the minority may state its dissenting views in the opinions.

(5) The Monopolies Commission shall prepare an opinion every two years on or before June 30, the first opinion to be prepared on or before June 30, 1976, covering the conditions prevailing during the last two preceding full calendar years, and transmit it to the Federal Government without undue delay. The opinions pursuant to sentence 1 shall be presented without undue delay by the Federal Government to the legislature and shall at the same time be published by the Monopolies Commission. The Federal Government shall comment to the legislature on these opinions without undue delay. In addition thereto, the Monopoly may in its discretion prepare additional opinions. The Federal Government may request the Monopolies Commission to deliver additional opinions. The Monopolies Commission shall transmit the opinions pursuant to sentences 4 and 5 to the Federal Government without undue delay and shall publish them. The Federal Minister of Economics may also request an expert opinion from the Monopolies Commission in individual cases which are before him for decision pursuant to § 24 (3).

(6) The members of the Monopolies Commission shall be appointed by the Federal President upon designation by the Federal Government. One member shall retire from office as of July 1 of each year in which an opinion is to be rendered pursuant to subsection (5), sentence 1. The order of retirement shall be determined by lot in the first session of the Monopolies Commission. The Federal President shall, upon designation by the Federal Government, from time to time appoint a new member for a term of four years. Reappointments shall be permitted. The Federal Government shall consult the members of the Monopolies Commission before it designates new members. The members shall be entitled to resign from office by giving notice to the Federal President. In the event that a member leaves prematurely, a new member shall be appointed for the term of office of the retired member; sentences 4 to 6 shall apply analogously.

(7) The resolutions of the Monopolies Commission shall require the approval of at least three members. The Monopolies Commission shall elect a chairman from its members. The Monopolies Commission shall adopt its own rules of procedure.

(8) The Monopolies Commission shall be provided with a secretariat. The function of the secretariat shall be the procuring and compiling of source materials, the technical preparation of

sessions of the Monopolies Commission, and the printing and publication of the opinions as well as attending to such other administrative matters as may occur.

(9) The members of the Monopolies Commission and the staff of the secretariat shall be obligated to keep secret the deliberations as well as the working papers which have been designated as confidential by the Monopolies Commission. The duty of secrecy shall extend also to information which is given to the Monopolies Commission and is designated as confidential.

(10) The members of the Monopolies Commission shall receive a lump sum compensation as well as reimbursement of their travel expenses. These shall be determined by the Federal Minister of Economics subject to agreement by the Federal Minister of the Interior. The costs of the Monopolies Commission shall be borne by the Federation.

Other provision of the GWB relevant to merger control, but not included in Part Three of the GWB

§ 46

Rights of Information and Investigation

(1) Insofar as required for the exercise of the functions of the Cartel Authority under this Act, the Cartel Authority may

1. demand information from enterprises and associations of enterprises regarding their economic conditions;
2. inspect and examine business records at the enterprises and associations of enterprises during normal business hours;
3. demand information from business and professional associations regarding the articles of association and resolutions, as well as the number and names of members to whom the resolutions apply.

(2) Owners of enterprises or their representatives, and in the case of legal entities, partnerships or associations without legal personality, persons designated as legal representatives by law or by articles of association, as well as representatives who have been appointed in accordance with § 36 (2), shall be obligated to furnish the information demanded, to submit business records and to permit the examination of these business records as well as the entry into offices and business premises.

(3) Persons who are commissioned by the Cartel Authority to make examinations may enter the offices of enterprises and associations of enterprises. The basic right of Article 13 of the Constitution is insofar restricted.

(4) Searches may be made only by order of the judge of the Local Court competent for the district where the search shall be made. §§ 306 to 310 and 311a of the Code of Criminal Procedure shall apply analogously to an appeal from such order. If danger of delay exists, the persons referred to in subsection (3) may conduct the necessary searches during business hours without judicial order. At the place of the search, a record of the search and its material results shall be made which, in the case that no judicial order was issued, shall also show the facts which led to a supposition of danger or delay.

(5) A person obligated to furnish information may refuse to answer questions if the answer would expose himself or a relative, as defined in § 383 (1), Nos. 1 to 3, of the Code of Civil Procedure, to the danger of criminal prosecution or of proceedings pursuant to the Act on Administrative Offenses.

(6) The Federal Minister of Economics or the highest state authorities shall call for information by means of an individual written order; the Federal Cartel Office shall call for it by means of a decree. The legal basis, the subject matter and the purpose of the request for information must be specified therein and a reasonable time period within which the information is to be furnished must be determined.

(7) The Federal Minister of Economics or the highest state authority shall order the

examination by means of an individual written order; the Federal Cartel Office shall order it by means of a decree with the consent of the President. The time, the legal basis, the subject matter and the purpose of the examination must be contained therein.

(8) *(repealed)*

(9) Knowledge and records obtained either through information received pursuant to subsection (1), Nos. 1 and 3, or through measures taken pursuant to subsection (1), No. 2, may not be used for tax proceedings or administrative fine proceedings concerning administrative tax offenses or exchange control contraventions; the provisions of §§ 93, 97, 105 (1), 111 (5) in connection with § 105 (1), and § 116 (1) of the Basic Tax Code shall not be applied to that extent. Sentence 1 shall apply neither to proceedings concerning criminal tax offenses and tax proceedings connected therewith if cogent public interests require their implementation nor in the event of the willful giving of wrong information by the person obligated to give information or by persons acting for him.

§ 48

Organisation of the Federal Cartel Office

(1) A Federal Cartel Office shall be established as an independent Superior Federal Authority with its seat in Berlin.

(2) Decisions of the Federal Cartel Office shall be made by the Decision-units, which shall be established and determined by the Federal Minister of Economics. Otherwise, the President shall determine allocation and operation of business of the Federal Cartel Office by means of rules of operation; they shall require confirmation by the Federal Minister of Economics.

(3) The Decision-units shall decide in bodies composed of a Chairman and two Associates.

(4) Chairmen and Associates in the Decision-units must be civil servants appointed for life. Chairmen and Associates must be qualified to serve as judges or in senior administrative positions; Chairmen should, as a rule, be qualified to serve as judges.

(5) The members of the Federal Cartel Office may not be owners, managers or members of the board of management or of the supervisory board of an enterprise, a cartel or a business or professional association.

§ 49

General Directives of the Minister of Economics

Insofar as the Federal Minister of Economics issues general directives to the Federal Cartel Office with regard to the issuance of or the abstention from issuance of orders pursuant to this Act such directives shall be published in the Federal Gazette.

§ 62

Right of Appeal

(1) Appeal from orders of the Cartel Authority shall be permissible. It may also be based upon new facts and evidence.

(2) Appeal shall be open to participants in proceedings before the Cartel authority (§ 51 (2) and (3)).

(3)

(4) Decisions on an appeal shall be made exclusively by the Court of Appeals competent for the district where the Cartel Authority has its seat, and in cases of §§ 24 and 24a, exclusively by the Court of Appeals competent for the district where the Federal Cartel Office has its seat, and even if the appeal is from an order of the Federal Minister of Economics. § 36 of the Code of Civil Procedure shall apply analogously.

§ 73**Second appeal on points of law**

(1) Appeals on points of law to the Federal Supreme Court from the decrees of the Court of Appeal on the merits shall be permissible, if the Court of Appeals has granted leave to appeal on points of law.

(2) Leave to appeal on points of law shall be granted if

1. a question of law of fundamental significance is concerned; or
2. the development of the law and maintenance of uniform decision practice require a decision of the Federal Supreme Court.

(3) The decision of the Court of Appeals must state whether leave to appeal on points of law is granted or not. If it is not granted, a statement of reasons shall be required.

(4) Granting of leave to appeal on points of law from decisions of the appellate courts shall not be required if one of the following defects in the proceedings existed and has been raised on appeal:

1. if the court making the decision was not constituted according to provisions of law,
2. if a judge, who was excluded by law from his judicial office or was successfully refused for fear of his being prejudiced, participated in the decision,
3. if a participant was refused his right to be heard,
4. if a participant was not represented in the proceedings according to provisions of law, unless the consented explicitly or implicitly to the conducting of the proceeding,
5. if the decision was made on the basis of an oral hearing in which the provisions regarding public proceedings were violated, or
6. if the decision does not contain a statement of reason.

§ 73**Second appeal on points of law**

(1) The refusal to grant leave to appeal on points of law may be appealed independently by an appeal from failure to grant leave.

(2) The decision regarding the appeal from failure to grant leave shall be made by the Federal Supreme Court in the form of decree which must contain a statement of reasons. The decree may be issued without an oral hearing

(3)

§ 98 (2)**Scope of Territorial Application**

(2) This Act shall apply to all restraints of competition which have effects within the territory in which this Act applies, even if they are caused outside the territory in which this Act applies. It shall also apply to export cartels within the meaning of § 6 (1) insofar as enterprises are participating in them which maintain their legal residence within the territory in which this Act applies.

Checklist for Merger Control Procedures

- Federal Cartel Office, Berlin 1990 -

- I. **Single Firm market domination**
 - 1. Market share
 - 2. Financial Strength
 - 3. Access to supply or sales markets
 - 4. Interlocks
 - 5. Barriers to market entry
 - 6. Competition from imperfect substitutes
 - 7. Foreign competition
 - 8. Buying power on the opposite side of the market
 - 9. Market phase
 - 10. Overall appraisal of competitive conditions
- II. **Oligopolistic market domination**
 - A. *Competitive conditions*
 - 1. Market share
 - 2. Symmetry of the oligopoly
 - 3. Interlocks
 - 4. Barriers to market entry
 - 5. Competition from imperfect substitutes
 - 6. Foreign competitors
 - 7. Buying power on the opposite side of the market
 - 8. Market phase
 - 9. Overall appraisal of competitive conditions
 - B. *Competitive process*
 - C. *Relationship between the oligopolies and outsiders*

I. Single Firm Market Domination

Introductory Remarks

The Act Against Restraints of Competition (ARC) offers a double definition for single-firm market domination. Accordingly, an enterprise is either market-dominating, if it is not exposed to any competition or to any substantial competition, or if it has a paramount market position in relation to its competitors. A paramount market position follows in particular from the market share, the financial strength, the access to the supply or sales markets, the links with other enterprises as well as the market entry barriers (Section 22 (1) of the ARC).

The second alternative, where the conditions of competition (market structure) are the decisive element, is of greatest practical importance in merger control, and there it is primarily discussed in this checklist. The first alternative, for which the competitive process (market conduct) is of crucial importance, primarily covers extreme cases of market dominance (see Bundestags-Drucksache VI/2520 p. 21) and is therefore not discussed specifically below.

To establish market domination as a result of a paramount market position, the ARC requires an overall appraisal of all the conditions of competition relevant to the market affected by the merger (BGH WuW/E 1504 "GKN-Sachs"). The competitive process in principle is of no importance for the finding of a paramount market position. A paramount market position is, in particular, not precluded by the existence of substantial competition (BGH WuW/E 1449 "Valium").

A *paramount market position* is present, if an enterprise, due to market- or firm-related structural criteria, has a scope of action which is not sufficiently controlled by its competitors. If the enterprise is able to use parameters of competition or pursue market strategies without having

regard to its competitors, there is at least a danger of the essential functions of competition being no longer fulfilled. The same applies, if such a competitive effect arises without the enterprise engaging in conduct to that end (Section 22 (1) No. 2, Section 24 (1) of the ARC; BGH WuW/E 1506 f "GKN-Sachs").

A paramount market position is strengthened through a merger, if the merger further deteriorates the conditions of competition on the market concerned. After establishing a paramount market position, it has to be examined whether the already existing scope of autonomous action is widened and workable competition thus becomes even less likely (BGH WuW/E 1691 "Springer-E. Wochenblatt"). Such strengthening effect is already present, if the enterprise after the merger is better able to fend off imitation competition and thus in a position to maintain or secure its paramount market position (BGH WuW/E 1536 f "Erdgas Schwaben"). The standard of proof to establish a strengthening effect is lower, the more extensively the market concerned is already dominated.

A paramount market position is created by a merger, if an enterprise thereby gains a scope of action in the affected market which is no longer sufficiently controlled by its competitors. What matters here is the post-merger conditions of competition. A prognosis of the conduct of the merged firm is not necessary. In the event of substantial pre-merger competition, however, there must be a strong probability that such competition will no longer take place in future (BGH WuW/E 1755 "Kläckner-Becorit").

The following firm- and market-related conditions of competition allow to draw conclusions as to the likelihood of an enterprise having a superior scope of action in the market affected by the merger. This is due to the fact that certain types of conditions of competition imply a typical kind of conduct given reasonable considerations and motivations of the enterprises (BGH WuW/E 1510 "GKN-Sachs"). The listing is not exhaustive and not all of the criteria mentioned are meaningful for every market. Mentioned are only some frequently occurring or normally meaningful conditions of competition.

1. Market share

The market share characterises the current market position and significance of an enterprise and provides information on its possible scope of action. A significant market share suggests a paramount market position. If there are also barriers to entry in the market concerned, single-firm market domination is likely to exist. A market share assessment is particularly meaningful, if besides the absolute size of the market share (a), the difference between the market share of the enterprise concerned and that of its largest competitor as well as the distribution of market shares generally (b) and the development of market shares in time are ascertained and evaluated (c).

a. The higher the absolute market share of an enterprise, the greater the likelihood that it has a not sufficiently controlled scope of action. The higher the market share of an enterprise, the higher also its ability to restrict competition in the market concerned. The enterprise will, in particular, be able to determine the price of the relevant product or service by changing its own supply or its own demand.

If the market share of an enterprise attains or exceeds the 33 1/3 per cent threshold, a restrictive influence on competition is particularly likely and single-firm market domination is presumed (Section 22 (3) No. 1 of the ARC). At the same time this raises the standards of proof to establish that contrary to the presumption there is no paramount market position. They are the higher, the more clearly the one-third threshold is exceeded.

The finding of a paramount market position does not depend on the existence of a market share of at least 33 1/3 per cent. Enterprises with smaller market shares may also be dominant, provided other conditions of competition create a paramount scope of action (Section 23a (1) No. 1a of the ARC; KG WuW/E OLG 2889 ff. "Krupp-Total").

b. The greater the difference between a firm's market share (or relative market share) and that of its largest competitor and the more fragmented the market shares of its other competitors, the greater the likelihood that the market (share) leader has a scope for restrictive action (BGH WuW/E 2155 f. "Rheinmetall-WMF"). Moreover, absolute and relative market shares are

interdependent. The absolute size of the market shares loses importance, as the market share difference widens and the market share structure is otherwise atomistic (KG WuW/E OLG 2863 f. "Rewe-Florimex").

These two criteria provide information on the competitors' ability to offer the other side of the market alternative choices, should the market leader use his scope of action to restrict competition. Relevant evidence can be supplemented by findings regarding competition production capacities and their degree of utilisation (KG WuW/E OLG 1752 "GKN-Sachs"). The larger the number of competitors and the smaller their market shares, the greater the likelihood of their adjusting to the market leader's competitive behaviour and thus the the existence of an uncontrolled scope of action.

A paramount market position is to be presumed *prima facie*, if

- the absolute and relative market share of an enterprise are significant,
- the supply is otherwise heavily fragmented, and
- all other conditions of competition are not in conflict with the presumption.

This applies also if the above-mentioned conditions are created as a result of a merger with a competitor and consequently the creation of a paramount market position it be expected (so-called "purely structural case"; BGH WuW/E 1755 f. "Klöckner-Becorit").

If the conditions of a purely structural case are not satisfied, the matter turns on the question whether the market share obtained by the merged enterprises as a result of the merger provides them with a scope of action no longer sufficiently controlled by their competitors. In principle the market share of merged enterprises amounts to the sum the market shares previously held by them separately. If the enterprises concerned do not form an economic unit as a result of the merger (Section 23 (1) sentence 2 of the ARC), as a rule internal competition between them is excluded, though. Market share losses due to a shift of customers to other suppliers are particularly unlikely, if the range of supplies firmly established in the market is fully retained (KG WuW/E OLG 2138 "Klöckner-Becorit").

If an enterprise already holds a dominant position in the market concerned due to its significant market share, that position can be strengthened even through minor increases in market share as a result of a horizontal merger (BGH WuW/ 1659 "Alsen Breitenburg-Klöckner").

c. The development of market shares over time can also be indicative of the presence or absence of a paramount market position. Competition is a dynamic process of initial moves of one competitor and responses of others to catch up with him. Accordingly, the market shares of enterprises in principle fluctuate over time. A persistently large market share consequently is an indication that there is an uncontrolled scope of action (BGH WuW/E 1504 "GKN-Sachs"). Market share fluctuations combined with changing market leadership or sustained heavy market share losses speak against its existence.

However, the possible causes of the market share development must always be considered, too. Market share losses in situations of intense price competition make market dominance unlikely (KG WuW/E OLG 2534 "Springer-az").

2. Financial Strength

Paramount financial strength may provide a firm with a scope of action, in particular as regards the use of parameters of competition such as price, capital spending, research, and advertising. Paramount financial strength results in a paramount market position if it has a discouraging or deterrent effect on competitors in the sense that it prevents actual competitors from engaging in active competition and potential competitors from entering the market ("resources" theory; BGH WuW/E 1510 f. "GKN-Sachs").

Single-firm market domination owing to financial strength is especially likely to occur if a firm also has a significant market share and if there exist barriers to entry that do not result from the firm's deterrent potential alone.

the discouraging and deterrent effects that may be caused by financial strength can also be produced by other resources such as R&D (BGH WuW/E 2356 "Daimler-MBB"), technological

and business know-how (BGH WuW/E 1751 "Klöckner-Becorit") as well as resources that are specific to a particular industry or market (BGH WuW/E 1858 ff. "Springer-Münchener Zeitungsverlag").

a. A firm's *financial strength* is determined by its possibilities of equity and debt financing. It may be assessed by measures such as turnover, profit, cash flow, net operating margin, credit line, access to national or international capital markets, and other criteria. Turnover is the criterion for instituting proceedings based on the legal presumptions as to market penetration, combined market dominance, and size in Section 23a (1) of the ARC. High turnover, however, is not always tantamount to high earnings. Therefore, it may not in every case be sufficient to consider turnover alone (BGH WuW/E 2582 "Kampffmeyer-Plange"). On the other hand, losses in one field of operation and a prolonged recession alone will not deprive a firm of its financial strength (BGH WuW/E 1756 "Klöckner-Becorit").

the financial resources of other enterprises may be added to those of the merging firms only if the former and the latter form an economic unit (Section 23 (1) sentence 2 of the ARC) - as a result of the merger, as the case may be. Links with financially strong firms may also have to be taken into account (BGH WuW/E 2582 "Kampffmeyer-Plange").

A paramount market position owing to financial strength is to be taken into account only if the financial power of the firm concerned exceeds that of its competitors. The stronger its resources, the greater its potential for predatory and disciplinary action, and the more likely single-firm market domination is to occur, provided that financial strength can be brought to bear on the market concerned (b. infra). The existence of financially strong competitors does not preclude a paramount market position of the merging firms (BGH WuW/E 1512 "GKN-Sachs"). It may, e.g., be unlikely that those competitors actually use their financial resources, a conclusion possibly to draw if their market shares have persisted at competitively insignificant levels for some time (BGH WuW/E 2581 "Kampffmeyer-Plange").

b. *Discouraging and deterrent effects* of paramount financial strength on competitors are to be expected if the competitors believe that the merging firms are likely to use those superior resources.

A firm may use its financial strength on most product and service markets for all kinds of purposes. Financial strength is likely to be used on appropriate markets if it allows predatory or disciplinary strategies to be successfully applied. A precondition for such strategies is that the financially strong firm disposes of free production capacity for increasing supply at short term. Further indications are given, inter alia, by the buyer's possibilities of changing to other suppliers, the ability of competitors to react successfully with parameters other than those relating to financial strength, and the significance of the market concerned to the overall operations of the financially strong enterprise. The existence of entry barriers and the market phase are also of special importance to the successful use of predatory and disciplinary strategies.

It is particularly difficult to prove anticompetitive effects of paramount financial strength if a paramount market position results from a pure conglomerate merger. This is most likely to happen on markets of mainly small and medium-sized firms, even if the merging firms have low market shares (Section 23a (1) No. 1a of the ARC; BGH WuW/E 2251 "Springer-Schleier Verlag"). The burden of proof is less heavy where existing market domination is further increased. This is very likely to occur if a market-dominating firm with a significant market share gains additional financial strength (Section 23a (1) No. 1b of the ARC). A dominating market position is strengthened in particular if the acquiring firm has already been competing with the acquired firm on neighbouring product markets ("market extension" merger; BGH WuW/E 1511 "GKN-Sachs") or if the merger serves to pursue particular business policies which may be reflected in an influx of capital, or in capital spending and expansion plans (BGH WuW/E 2157 "Rheinmetall-WMF").

3. Access to supply or sales markets

A firm's easier access to the supply or sales markets for goods and services and relation to its competitors may give the firm considerable scope of action in the market concerned and allow it to occupy a paramount market position. A paramount market position is present, in particular, if

based on its easy access to the supply or sales markets, a powerful firm (in terms of market share) may make access to such markets difficult for its rivals or even impossible (market foreclosure effect). This is also true, if the effect of market foreclosure occurs without the firm having adopted any behaviour to that end. Potential competitors perceive this restraint of competition as higher barriers to market entry.

The effect of market foreclosure occurs above all, if a firm is engaged not only in the market concerned but also in an important upstream or downstream market (vertical integration) and occupies at least powerful positions in both markets (a.). A restraint of competition similar to the market foreclosure effect, but usually less severe may be caused by the supply of a full line of products. This applies only if the suppliers' rivals offer a less wide range of products and services or none at all (b.). Access to the sales markets may also be made difficult for rivals, where a diversified firm is in a position to promote its sales in the market concerned by means of reciprocal dealing (reciprocity) (c.). Finally, resource-based competitive advantages may give a firm easy access to the supply or sales markets (d.). Unlike vertical integration, the latter three restraints of competition alone as a rule cannot give rise to a paramount market position. Rather, other structural factors, in particular market share, must also be present. However, the supply or rounding off of a full line of products, reciprocal dealing or the resource-based competitive advantages which result from a merger are likely to strengthen a paramount market position.

a. A paramount market position of a vertically integrated firm is the more likely, the higher its absolute and relative shares of the market concerned and of an important upstream or downstream market. Market foreclosure effects are likely, in particular, if important competitors depend on supplies from (BKartA WuW/E 1722 "BP-Gelsenberg") or sales to (BKartA WuW/E 2346 f. "Daimler-MBB") the vertically integrated firm. They may also occur, if the vertically integrated firm holds a market position in the supply or sales market.

Market foreclosure effects resulting from a vertical merger strengthen as a rule the market position of the merging enterprises. They may result in the creation of a paramount market position. They are very likely to strengthen the paramount position already held in the market concerned (BGH WuW/E 1769 "Teerbau-Makadam"). For such links between enterprises strengthen a dominant position by making innovative competition even more difficult for vertically non-integrated competitors and raising the barriers to entry for potential competitors. This is all the more true, where the merger occurs between two firms that dominate their respective levels of the market (BKartA WuW/E 2346 "Daimler-MBB"), in which case as a rule this market position is deemed to be strengthened.

Paramount market positions resulting from vertical integration may occur not only, if a firm is engaged at two levels of a market at a time, or if two firms operating at different levels of the market form an economic unit (Section 23 (1) sentence 2 of the ARC). Easy access to the supply or sales markets may also be due to links with suppliers or buyers (BGH WuW/E 2581 "Kampffmeyer-Plange"; BKartA WuW/E 1912 f. "Lufthansa-first"). For even if a firm holds a minority share in a supplier or buyer, preference will always be given to the latter, unless its rivals submit more favourable offers (BGH WuW/E 1768 "Teerbau-Makadam").

A supply relationship which existed before a vertical merger between the parties in principle does not preclude the creation or strengthening of a paramount market position (BGH WuW/E 1952 f. "Braun-Almo"). A supply relationship generally does not result in the parties cooperating as closely as they would if they merged, nor is such a relationship as durable as a merger.

b. Easy access to the sales market as a result of a firm offering a *full line* mainly of complementary and substitute products presupposes that there is a regular demand for the relevant goods and services from a competitively significant number of buyers, and that no other firm offers a comparable range of goods. This applies similarly to the supply of turnkey (production) plants or package deals. The supply of a full line of products or of turnkey plants will restrict competition primarily if the buyers may achieve economies of scope by concentrating their purchases on the supplier of the full line or if the supplier, due to his market power in a submarket of that line of products, may cause buyers to concentrate their purchases on him, e.g. by means of tie-ins. Such predatory competition at the cost of one-product firms may be engaged in not only by diversified suppliers operating in several product markets, but also by firms that offer goods or services belonging to the same product market in a wide range of price and quality (KG WuW/E OLG 3762 "Pillsbury-Sonnen Bassermann").

Easy access to the sales market based on the supply of a full line of products may significantly

enlarge a firm's scope of action in the market concerned, but does not, as a rule, allow it to engage in independent action that is no longer controlled by competitors. For this to be possible, there must be additional factors, primarily a significant market share. This applies equally to conglomerate or horizontal mergers which enable a firm to offer a full line of products for the first time. However, if a firm already has paramount market position in the market concerned, that market position may be strengthened by a merger allowing the firm to offer or round off a full line of products (BKartA WuW/E 2418 "WMF-Hutschenreuther"). The paramount market position is likely to be strengthened if the other merging firm has a strong position (in terms of market shares) in a submarket of the line of products (BKartA WuW/ 1855 f. "IBH-Wibau"). A strengthening of the paramount market position may be assumed to occur if the merging firms are market-dominating in their respective submarkets (BKartA WuW/E 2331 f. "Messer Griesheim-Buse").

c. Easy access to the sales market as a result of reciprocal dealing presupposes that a firm makes purchases from its customers in a third market. The number of those customers must be significant in terms of competition in the market concerned. Competition will be restricted if those customers grant the diversified firm preferential treatment over its competitors in purchasing in the market concerned, but may not by itself create a paramount market position. This applies also to conglomerate mergers allowing reciprocity. However, if a paramount market position already exists in the market concerned, it may be strengthened by a merger providing a possibility of reciprocal dealing. The paramount market position is likely to be strengthened if the other firm involved in the merger may cause a significant number of buyers to purchase from the market-dominating supplier (BKartA AG 81, 290 "Südzucker-KWS") or is itself market-dominating as a buyer.

d. Easy access to sales or supply markets owing to a firm's resource-based competitive advantages may result from, among other things, a good reputation or acceptance in the market (BGH WuW/E 1504 "GKN-Sachs"), a dense network of own outlets (BGH WuW/E 2156 "Rheinmetall-WMF"), a large number of production plants that allow to supply a large area, or a secure supply of raw materials (BGH WuW/E 2581 "Kampffmeyer-Plange"), a network of own correspondents (BGH WuW/E 1757 f. "Springer-Münchener Zeitungsverlag"), or an own chain of first-rate hotels (BKartA WuW/E 2178 "TUI-Air Conti"). Resource-based competitive advantages of a firm may also to a limited extent be an obstacle to other firms' access to supply or sales markets. This will substantially increase the likelihood that a firm which also has significant market shares enjoys a paramount market position. To the extent that such a position already exists, it may be strengthened by a merger that improves the market-dominating firm's access to upstream or downstream markets (BKartA WuW/E 2376 "Melitta-Kraft").

4. Interlocks

Interlocking directorates and interlocking capital arrangements among firms, in particular with competitors, customers or suppliers may be contributing factors of a paramount market position, but may not lead to its creation. Restraints of competition resulting from interlocks are largely covered by other structural criteria contained in this checklist. Thus, interlocks with financially powerful firms may enlarge a firm's financial scope, and interlocks with customers or suppliers may secure sales outlets or sources of supply as well as increase barriers to market entry. This criterion is significant in the case of interlocks with competitors.

Interlocks with actual or potential competitors as well as with suppliers of imperfect substitutes as a rule restrict competition among those competitors. Unilateral and cross minority holdings or joint ventures generally result in mutual consideration of the other party's interests. They may also enable firms to prevent other companies in which they hold participations from engaging in competitive action that would place them at a disadvantage.

5. Barriers to market entry

Barriers to entry are an indication of the importance of potential competition to the competitive process on the market concerned. As long as a powerful firm is unable to quote excessive prices or cannot dispense with R&D because other potential competitors would be likely to enter

the market, the latter have a controlling effect on the powerful firm's scope of action, and single-firm market domination cannot be assumed to exist. However, if barriers to entry prevent potential competition from effectively controlling the powerful firm's freedom of action, it is far more likely that the latter enjoys a paramount market position. High entry barriers in principle restrict potential competition (a.).

If there are no barriers to entry or if entry is easy, it is likely that potential competition exists.

By merging with a potential competitor, an established powerful or market-dominating firm may substantially increase or secure its scope of action (b.).

a. Barriers to market entry are legal or economic obstacles hindering firms outside a market from entering it. Such obstacles may actually exist for all potential new entrants, or they may render market entry based on reasonable commercial considerations and motives unlikely. They need not preclude market entry, nor need they exist indefinitely. It is enough if they delay or impede market entry for a competitively significant period of time.

Entry barriers consist in particular in

- *Statutory restrictions of market entry*

Legal provisions may restrict market entry or the use of certain parameters by firms and thereby decrease potential competition in favour of the established firms. Examples are conditional authorisations for environmentally harmful plants (BKartA WuW/E 1758 "Teerbau-Makadam") or for the operations or rates of transport companies or public utilities. The same applies to limited resources owned by established firms, e.g. raw or waste materials deposits, locations, airport slots, patents. Technological constraints on the absorptive capacity of downstream markets may also constitute barriers to entry (BKartA WuW/E 1949 "Morris-Rothmans").

- *Economies of scale*

Economies of scale enjoyed by established firms in R&D, production (BGH WuW/E 1504 "GKN-Sachs") or the marketing of their products (BKartA WuW/E 2328 "Messer Griesheim-Buse") may render market entry unlikely for factual reasons. Economies of scale arise as costs of R&D, production or marketing decrease with growing firm size. New entrants will in general secure only small initial market shares. The greater the market share that is required to achieve the same economies of scale as the established competitors, the higher the barriers to entry due to the necessary initial capital requirements and risks to be borne by new entrants.

The same applies to *economies of scope* that are often realised by diversifying firms. Economies of scope arise if one firm is engaged in different commercial activities at lower costs than would be incurred if different firms carried on each activity separately. This includes advantages of vertically integrated firms that may require a new entrant to enter the market at more than one level at the same time.

- *Strategic barriers to entry*

By their market conduct, established firms may erect factual entry barriers for new entrants and thereby render entry more difficult for them. The practice of all manufacturers of a particular market to conclude exclusive dealing contracts with their customers (Section 18 of the ARC) is an example of strategic entry barriers (BKartA WuW/E 2215 f. "Linde-Agefko"). Demarcation and concession agreements with public utilities (Section 103 (1) of the ARC; BKartA WuW/E 2157 f. "EVS-TWS") or industry-wide (Section 5 (1) of the ARC) or individual firms' standards for complementary goods have similar effects.

Strategic barriers to entry may also exist in the form of buyer preferences for established suppliers insofar as the preferences have been created by advertising and inter-brand competition.

- *Deterrent potential of market leader*

A substantial market-strategic or resource-based deterrent potential of the market leader on the market concerned may also limit potential competition and render market entry by similarly situated firm unlikely (BGH WuW/E 1510 "GKN-Sachs"). Even if this does not preclude market entry, new entrants may be deterred by the ability of established firms to keep them from attaining a competitively significant market position. A substantial deterrent potential exists, e.g., if the market leader owns considerable market-specific resources (BGH WuW/E 2283 "SZ-Donau Kurier"), if it has financial strength on a market characterised by advertising and inter-brand competition (KG WuW/E OLG 3079 "Morris-Rothmans"), if it is interlinked with major customers (BGH WuW/E 1769 "Teerbau-Makadam"), or if it has a market-dominating position on substantial geographic submarkets (BGH WuW/E 1860 "Springer-Münchener Zeitungsverlag"). In all these cases the market leader has a paramount market position even before any new entry occurs - also in relation to potential competitors. For this reason, significant market shares or a high degree of concentration may themselves constitute high barriers to entry.

- *Market trends*

Market entry is the more likely to occur, the higher the future profit prospects are expected to be. New and growing markets or markets with excess demand therefore have lower barriers to entry than have stagnant markets with excess capacities.

The success or failure of pre-merger entry may be an indication of the competitive significance of barriers to entry into the market concerned. Market entry suggests the existence of substantial potential competition, unless - measured by the new entrants' market shares - it has remained competitively insignificant (KG WuW/E 2836 "Holtzbrink-Rowohl", on the one hand, and 2865 "Rewe-Florimex", on the other). Where market entry failed or no entry was made, even though the new entrants met all the necessary conditions of successful market entry, it may be assumed that entry barriers exist.

b. If the freedom of action of an established powerful firm is only effectively controlled by potential competitors, merger with a potential competitor may provide the established firm with a paramount market position (BKartA WuW/E 1649 f. "Erdgas Schwaben"). If the established firm already has a paramount market position, it will as a rule be strengthened by *any merger with a significant potential competitor*, because possible improvements in the conditions of competition are thereby rendered less likely (BKartA WuW/E 1724 "BP-Gelsenberg"). Potential competitors are among others, firms which clearly intend to enter the market (BKartA WuW/E 1723 "BP-Gelsenberg"), which produce relevant goods or services for in-house consumption (BKartA WuW/E 2249 "Hüls-Condea") or supply them on nearby markets, which can easily use their capacities for the production of other goods or services, or which are on up-stream or downstream markets (BGH WuW/E 1952 "Braun-Almo").

Potential Competition may also be restricted by vertical or conglomerate mergers. However, this restraint of competition is only a side-effect of vertical integration or strengthened resources and therefore does not by itself lead to the creation or strengthening of a paramount market position.

6. Competition from imperfect substitutes

Competition may come from goods or services which, though in the eyes of buyers being imperfect substitutes for those of the market concerned, may replace them to a limited extent or under certain conditions (a.). Competition from imperfect substitutes therefore in principle plays an important role only as a form of residual competition in a market already characterised by a paramount market position. Consequently, a restraint of competition as a result of a link-up of an enterprise operating in the market concerned (primary market) with a substitution rival as rule can only strengthen already existing market dominance but not result in creating it (b.). On the other hand, competition from imperfect substitutes may not be so significant as to preclude the

presence of a paramount market position.

a. *Goods or services* may be imperfect substitutes for various reasons. For example, a shift to an imperfect substitute may be possible for buyers only in the long term, because they must make investments first to be able to actually use the substitute (e.g., when switching from electricity to gas as a source of energy). The choice of the imperfect substitute may imply a change in the taste or the habits of buyers (e.g. when shifting from a political weekly to a national daily). A change may also be burdensome owing to price differences in connection with the purchase or the use of the imperfect substitutes.

Several goods or services that belong to different product markets may serve as imperfect substitutes. The intensity of competition from imperfect substitutes may differ depending on how good a substitute on product might be for another from the buyer's point of view. In the case of heterogeneous products or services the intensity of competition from imperfect substitutes may differ also in respect of individual suppliers in the primary market (BGH WuW/E 2123 f. "G+J-Zeit").

b. Competition from imperfect substitutes in principle is a form of residual competition in dominated markets and may control the scope of action available to the enterprises involved only imperfectly. The presence of a paramount market position can thus be precluded only in exceptional cases, if, e.g. a completely new product which belongs to a different product market will replace the product in the market concerned in the foreseeable future. Just as competition from imperfect substitutes in principle does not preclude the presence of a paramount market position, the mere restraint thereof through a link-up of an enterprise in the primary market with a substitution rival does not lead to the creation of such a market position. Existing dominant positions may be strengthened thereby, though. Such a strengthening effect is likely to occur, if the dominant enterprise merges with a powerful (in terms of market shares) substitution rival (BGH WuW/E 1536 f. "Erdgas Schwaben"). This applies in particular, if the latter holds a paramount market position in the market for the imperfect substitute as well. It may then be assumed that after the merger both firms will be able to exert influence on or control over the extent and the intensity of competition from imperfect substitutes to their own advantage.

7. Foreign Competitors

The significance of foreign competitors to the domestic market conduct does not always correspond to that of domestic competitors. Participation of foreign competitors in domestic markets may depend on factors that are irrelevant to domestic competitors. Their market shares may therefore understate or overstate their competitive significance (a.). Potential foreign competition may be taken into account in exceptional cases only (b.).

a. *Actual foreign competitors* and domestic competitors in principle have to be treated the same. The market position of actual foreign competitors has to be determined according to the criteria used for domestic competitors. Their market shares have to be determined on the basis of their actual domestic shipments or sales. However, market shares might give a misleading impression of the actual significance of foreign competitors to the competitive conduct in the domestic market.

The competitive significance of foreign competitors may be greater than their actual domestic shipments indicate. This will be the case, for example, if the foreign supplier occupies a leading position in the world markets or if important domestic buyers have already done a great deal of business with the foreign competitor in foreign markets. In general, the competitive significance of firms with small market shares in the domestic market whose location or center of activities lies within the EC is greater than could be assumed from their market shares. However, the competitive significance of foreign competitors may be smaller than their actual domestic shipments suggest. This may be possible, in particular, if there are tariff and non-tariff barriers to trade, voluntary (export) restraints (BKartA WuW/E 2366 "Linde-Lansing") or if buyers give preference to domestic competitors (BKartA WuW/E 2250 "Hüls-Condea"). Generally speaking, the competitive significance of firms whose location or focus of activities lies outside the EC is smaller than is reflected by their shares of the domestic market. This is true, in particular, of firms from Socialist countries. Moreover, the domestic activities of foreign competitors may be limited for firm-specific reasons. The type and level of their domestic operations - e.g. mere imports or independent domestic production - or interlinks or cooperation with domestic competitors may

give a first indication.

b. *Potential foreign competition* as a rule is of very limited importance to domestic markets because the likelihood of market entry cannot be established with sufficient certainty. The absence of trade barriers and the presence of foreign competitors in adjacent geographic markets of other countries tend to be indicative of potential competition. An indication thereof does not suffice, however, for such competitors to be included as potential competitors (KG WuW/E 3079 "Morris-Rothmans").

8. Buying power on the opposite side of the market

The likelihood of a paramount market position increases in proportion to the degree of fragmentation of the other side of the market. Firms wielding buying power on the other side of the market by contrast may stand in the way of market domination by a single firm.

If a buyer accounts for most of the demand in a market, its buying behaviour can greatly influence competition among suppliers. There will be no supply-side market domination if the buyer's purchases are determined by strategic considerations rather than by the supplier's competitive conduct (BGH WuW/E 1752 "Klöckner-Becorit"). A strategic buying behaviour is likely if the supply market is of great importance to the buying enterprise, e.g., because the cost of the primary product essentially determines the selling price of the processed final product. On the other hand, placing orders according to quotas or in order to prevent exits from the market does not in itself constitute market-strategic demand. When making procurement decisions, public buyers generally have to take account of political rather than market strategy consideration; domestic firms are therefore given preference in most cases (BKartA WuW/E 2348 f. "Daimler-MBB"). As a rule, their buying power, if any, equally affects all suppliers and does not contribute to the maintenance of competition among suppliers.

Vertical integration or mergers between firms enjoying buying power and dominant suppliers as rule prevent adoption of market-strategic buying behaviour that promotes competition among suppliers.

If an oligopsony accounts for most of the demand, the same applies in principle as in the case of monopsony (KG WuW/E OLG 3763 "Pillsbury-Sonnen Bassermann").

9. Market phase

The market phase refers to the development stage of a market and hence to the stability of its competitive conditions. There is an essential difference between the two early market phases, the experimental stage and the growth stage (a.), and the two late stages, the maturity and the stagnation phases (b.). In principle, a paramount market position is more likely to exist in the late market phases than in the early ones.

The market phase is not so much an independent criterion as a criterion complementary to other conditions of competition.

a. In the *experimental and growth phases* of a market, competitive conditions undergo perpetual change and therefore are hardly indicative of any stable scope of action. While the relevant product or service has already found a market, it can still be greatly developed and improved; other possible uses may still be discovered. Many competition parameters may be used and rather than enticing away customers from competitors their use will create a new demand.

In these early market phases high market shares are not unusual, if not inevitable. From the growth phase onward, they will be dismantled by newcomers if there are no or low barriers to market entry. Economies of scale and buyer preferences caused by inter-brand and advertising competition alone do not constitute entry barriers. Financial strength is of minor importance, because an expanding market allows all firms the necessary scope. In addition, the use of financial resources can mostly be neutralised by other, usually technical resources. Upstream and downstream markets as a rule are open to all firms.

Nevertheless, paramount market positions are not impossible in the early market phases. Therefore, new markets are also subject to merger control (Section 24 (8) No. 3 ARC). The creation of paramount positions requires that - particularly as regards their research and development potential - the merging firms have a significant competitive edge over all their competitors which is unlikely to diminish even in later market phases. A paramount scope of action is likely in particular if a merger results in a market barrier to potential competitors (BKartA WuW/E 2146 "GfL").

b. In the maturity and stagnation phases the conditions of competition in the market concerned change more slowly, if at all. In relation to the general trend, the market growth is below average. Products and production processes can hardly be improved any further; all efforts are now being aimed at distribution. All possible uses of the relevant goods have been discovered and tested. Any remaining competition parameters can only be used to respond to competitors' moves. Therefore what tends to be used is the less easily imitable parameters. Instead of price competition there is a growing amount of competition on quality, service and advertising (BGH WuW/E 1509 "GKN-Sachs").

Since actual competitors in the market orient themselves by existing conditions of competition, large market shares are unlikely to decrease in later market phases. Competitive advantages which individual firms may enjoy - e.g. because of their superior financial strength or their easy access to the supply or sales markets for goods and services - render innovative competition more difficult and are likely to exclude disadvantaged or less highly integrated firms. New entry is rather unlikely, particularly if the market is stagnant (KG WuW/E 1752 "GKN-Sachs"). Competition is likely to resume only if as a result of innovations the market reenters an earlier market phase or definitely enters the phase of decline in which firms may try to reduce the costs of their market exit.

Paramount market positions are therefore likely to occur mainly in the two later market phases. While the mere fact that a market moves into a late phase does not pose a threat to competition, the chances that there will be post-merger competition can greatly diminish. This is also true of resumption of competition, if paramount market positions are created or strengthened in the late market phases as a result of mergers (KG WuW/E 3080 "Morris-Rothmans").

10. Overall appraisal of competitive conditions

In a final, overall appraisal all competitive conditions that are of significance to a particular market have to be examined to establish whether a paramount market position and hence single-firm market domination are likely (BGH WuW/E 1980 "SZ-Münchener Anzeigenblätter"). Market conduct should be taken into account only, if the conditions of competition alone give but a poor indication of the presence of a paramount market position (BGH WuW/E 1759 "Klößner-Becorit").

In the case of highly diversified firms with particularly great resources it may be necessary to analyse the spillover effects of their competitive potential which cross the lines of the market affected by the merger.

A paramount market position is very likely, if all *conditions of competition* considered either separately or together indicate that a firm's scope of action is no longer controlled by its competitors. Here the independent scope of action in relation to individual competitors may also derive from various structural criteria. In relation to competitors with financial strength, for example, a firm's scope of action may derive from its significant market share, whereas in relation to its mid-size competitors its scope of action may result from its easier access to the sales market.

However, very few factors or even a single one may suffice to indicate a paramount market position. Most relevant in this context are the structural factors market share - assuming a "purely structural case" (see I.1.b. supra) - and financial strength, particularly if one of the monopoly presumptions (Sections 22 (3) No. 1, 23a (1) ARC) applies. If both the market share and the financial strength of a firm provide evidence of its uncontrolled scope of action and if in addition there are barriers to new entry, a paramount market position is very likely. In the presence of this combination of competitive conditions, very ample evidence is required to rebut

the presumption of single-firm market domination. If a firm's market share and financial strength are insufficient evidence of its paramount scope of action, the remaining conditions of competition may still give the firm a decisive advantage over its competitors (KG WuW/E OLG 2889 f. "Krupp-Total").

What applies to competitive conditions as indicators of a paramount market position also applies to the conditions of competition which prevent a paramount market position. One single structural factor may be sufficient to rule out a firm's independent scope of action (KG WuW/E OLG 4105 "w+i Verlag-Weis Druck"). For instance, a firm's paramount scope of action as evidenced by a significant market share may be offset by a rival's financial strength. For as long as they have the necessary capacity reserves financially strong rivals may disrupt the market leader's monopolistic conduct considerably even if their market shares are small. Similarly, market specific resources of competition may prevent a firm gaining a paramount market position as a result of its paramount financial strength.

If a particular market is characterised by conditions of competition which indicate that a firm may or may not have an uncontrolled scope of action, without one structural criterion being sufficient evidence against a paramount market position, then those criteria must be appraised as they relate to each other. Again of special importance are the meaningful criteria market share, financial strength and barriers to entry. The greater the likelihood of an independent scope of action on the basis of those criteria, the greater the amount of evidence of offsetting factors that is required to rebut such an assumption.

If the appraisal of competitive conditions does not give a clear indication of the presence or absence of a paramount market position, the analysis has to include the actual market conduct so that the structural criteria can be better evaluated (BGH WuW/E 1716 "Mannesmann-Brueninghaus"). The presence of substantial competition in the market concerned in itself does not rule out the presence of a paramount market position (KG WuW/E OLG 2543 "Braun-Almo"). A paramount position can be excluded only if substantial competition in turn results from structural factors that are not affected by the merger (BGH WuW/E 1756 "Klöckner-Becorit").

If there is no sufficient evidence to show the presence or absence of a paramount market position even after the market conduct has been taken into account, and if the conditions for presuming market domination pursuant to Sections 22 (3) No. 1, 23a (1) ARC are met, then single-firm market domination can be concluded to be present on that basis (case of "non-liquet"; BGH WuW/E 1754).

Where the analysis involves the creation or strengthening of a paramount market position as a result of a merger, the appraisal has to compare pre-merger and post-merger conditions of competition in the market concerned. Also to be considered are the future trend of the market and further changes in the competitive conditions expected as a result of the merger, if competition is not restricted already upon completion of the merger (BGH WuW/E 1507 f. "GKN-Sachs").

It is rare for mergers to change competitive conditions (quantitatively) so profoundly that the appraisal reveals totally different conditions after the merger. This is particularly true when the creation of a paramount market position is the alternative to be analysed. However, the conditions of competition that remain unaffected by the merger are not decisive where other competitive conditions indicate a threat to substantial competition. In a market where barriers to new entry are present, a significant increase in market share concentration may already suffice.

If substantial competition has been found to exist prior to the merger, the analysis must determine whether the merger will change the conditions of competition so drastically that after the merger substantial competition no longer has the effect of preventing market power (BGH WuW/E 1755 "Klöckner-Becorit").

For example, this effect of substantial competition will no longer be present, if as a result of the merger the market strategy potential of a firm is substantially expanded or if the firm gains distinct competitive advantages over its rivals (KG WuW/E OLG 3764 "Pillsbury-Sonnen Bassermann"; 4173 "Kampffmeyer-Plange").

In a market fully dominated by a firm in a paramount market position, the effect of any deterioration in the competitive conditions on the market conduct is disproportionate. *Single-firm domination is more likely to strengthened*, the higher the intensity of the restraint of competition

already being practiced. For the greater the control over the market, the greater the need to protect what competition is left (BGH WuW/E 1860 "Springer-Münchener Zeitungsverlag").

In the case of highly diversified firms or firms with particularly great resources as well as in the case of giant mergers (Section 23a (1) No. 2 of the ARC), the examination has to include an analysis of possible spillover effects which cross the lines of the market affected by the merger. The substantial cumulation of resources of market-dominating positions and resources may have spillover effects and increase the likelihood of paramount market positions existing, being created or strengthened in the market concerned as a result of the merger. This can be assumed to occur, in particular, if due to the merger a firm accounts for a very large percentage of the production capacities and jobs of an economic sector, becomes the dominant industry leader and can use the resulting political influence at the expense of its competitors (BKartA WuW/E 3247 "Daimler-MBB"). Moreover, the competitive potential of a diversified firm may be increased considerably by the fact that its market positions and spheres of influence are respected by other large firms. For example, a large firm may use its financial strength with great restraint in markets in which it competes with another large firm or may altogether forego entry into markets in which a large firm already operates.

II. Oligopolistic Market Domination

To establish oligopolistic market domination for the purposes of merger control, the ARC requires an overall assessment of all the conditions of competition and the competitive process in the market affected by the merger of enterprises (BGH WuW/E 2027 "Texaco-Zerssen"). In principle

- in the market affected by the merger there must be conditions of competition which induce totality of firms (oligopoly) for forego competitive actions and facilitate conscious parallelism (A.),
- no substantial competition must exist among oligopolists (B.), and
- provided other firms (outsiders) are active in the market besides the oligopolists, no substantial competition must be left between the outsiders and the oligopolists. Alternatively, there must be a paramount market position of the oligopoly in relation to outsiders (Sections 22 (2), 24 (1) of the ARC) (C.).

Thus, for the purposes of an overall assessment, the competitive process and the conditions of competition in principle carry the same weight in establishing the presence of oligopolistic market domination. This is not so, if the conditions of the qualified oligopoly presumption are met (Section 23a (2) of the ARC). Then oligopolistic market domination is precluded by substantial competition only if substantial competition is still highly likely to take place in future in spite of unfavourable conditions of competition.

Where the analysis concerns the strengthening of oligopolistic market domination, it has also to be examined, in addition to the above-mentioned examination required in principle, whether the conditions of competition can be expected to deteriorate further. Forecasting of competitive conduct is not required. It is sufficient if the merger is highly likely to facilitate or secure parallel behaviour. The evidence requirements for establishing such a strengthening are the lower, the higher the degree of market concentration already reached.

Where the creation of oligopolistic market domination is concerned, the post-merger conditions of competition will be the deciding factor. An overall assessment of the post-merger conditions of competition must reveal that the oligopoly can be expected to adopt conscious parallelism in future. Again, conduct forecasting can be dispensed with. However, the substantial competition found or assumed to exist before the merger must be highly likely no longer to be present after the merger. The indicative effect of the presence of substantial competition before the merger is the smaller, the greater the change in the conditions of competition in the market concerned as a result of the merger.

The following three sections of this checklist are arranged in the same order as that provided by the legal definition of oligopolistic market domination (Section 22 (2) of the ARC). In a slightly different order, they may also be used to determine whether the qualified oligopoly presumption

(Section 23a (2) of the ARC) is rebutted. In checking the first alternative of rebuttal (the conditions of competition may be expected to leave substantial competition also following the merger), Part II.B. (competitive process) should be referred to first and then Part II.A. (conditions of competition). The second alternative of rebuttal (the oligopoly has no paramount market position in relation to outsiders) can be checked according to Part II.C. (relationship between the oligopolists and outsiders).

A. Competitive conditions

1. Market share

Often the market shares of the leading firms in a market and their distribution allow a (first) determination of the presence of a potentially market-dominating totality of firms (a.), as well as an assessment of the competitive process in the market affected by the merger (b.).

a. In finding out which firms are members of a market-dominating oligopoly and which firms should be considered outsiders, the line can be drawn in theory between those firms that use their parameters with the interests and reactions of other firms in mind, and those that can only passively adjust to such behaviour. If a market leader can afford to ignore even his largest competitors' reactions, then there is no oligopoly, but possibly single-firm market domination.

Since it is nearly impossible in practice to determine the decisive factor, firm-related structural criteria - such as market shares and differences between market shares and also resources, access to supply or sales markets etc. (KG WuW/E 4105 "w+i-Weiss-Druck") - are used to define the oligopoly and the outsiders as well as the oligopoly and the possible presence of single-firm market domination.

b. It is only above a certain degree of concentration of supply or demand in a market that the oligopolistic interdependence of firms will be perceptible. Competitive moves by individual firms will affect competitors and induce them to react. Increasingly, the potential reactions of competitors will be taken into account when a firm uses its parameters. The stronger the interdependence having already existed before or arising from mergers, the more likely are practices to avoid competition (conscious parallelism) and hence the exclusion of substantial competition.

The market share thresholds of the oligopoly presumptions (Sections 22 (3) No. 2, 23a (2) of the ARC) point to *tight oligopolies* in which the firms belonging to the oligopoly are very likely to take parallel courses of action. The exclusion of substantial competition from the oligopoly is the more likely, the tighter the oligopoly and the fewer the outsiders. As the degree of concentration decreases, the likelihood of parallel behaviour diminishes. Where the degree of market concentration falls significantly below the thresholds of the presumptions, conscious parallelism as rule can be expected to occur in transparent markets for homogeneous products.

The *development of market shares* of the oligopolists over time may also provide meaningful information about the competitive process. Stable or relatively stable market shares or differences between the oligopolists' shares point to an uncompetitive oligopoly. This is true, in particular, if market shares have remained stable despite significant changes in external market circumstances, such as a substantial drop in demand (BKartA WuW/E 2301 "Heidelberger Zement-Malik").

However, if market shares are so unstable that the firms hold different ranks with every new period it can be assumed that there is a competitive oligopoly. Short-term fluctuations in market shares (two-four periods) in principle are more meaningful than are long-term fluctuations. The former point to active competitive conduct, whereas the latter are more likely to result from structural changes of the market conditions such as a change in buyer preferences (KG WuW/E OLG 3075 f. "Morris-Rothmans"). However, the causes of the market share fluctuations also have to be considered. If they merely result from inter-brand and advertising competition without quality competition being also present, even market share fluctuations will give no indication of the presence of substantial competition (see II.B.2. *infra*).

If a *horizontal merger* results in substantial market shares being concentrated in the hands of the leading firms of the market affected by the merger, oligopolistic market domination will likely be

created. At any rate, this will occur, if the thresholds of the oligopoly presumptions are exceeded or reached (for the first time). As a rule, the oligopolistic interdependence will become so strong that strategies to reduce competitive pressure through parallel action become very likely.

Where a market-dominating oligopoly already exists, it is likely to be further strengthened by any subsequent horizontal merger which results in the oligopoly becoming tighter or outsiders joining the oligopoly. As the number of oligopolists decreases, the competitive conduct within the oligopoly as a rule becomes more transparent, which facilitates parallel behaviour. Mergers with outsiders will reduce the latter's ability to undertake competitive moves which might disrupt the parallel behaviour of the oligopolists. This occurs, in particular, where mergers take place with outsiders that are particularly efficient and the most likely source of competitive impulses (for "catch-up mergers" see II.A.2. *infra*).

2. Symmetry of the oligopoly

The more equal the firm-related structural characteristics of the firms belonging to an oligopoly are, the greater the likelihood of conscious parallelism will be (KG WuW/E OLG 3080 "Morris-Rothmans").

A symmetrical oligopoly consisting of firms with largely similar market shares, comparable resources and a comparable ease of access to the supply or sales market tends to be uncompetitive, since any competitive action would be equally perceptible to all firms, easily detectable due to the transparency of the competitive conduct, and hardly promising because all the firms have a similar retaliatory potential. An oligopoly that is symmetrical due to its vertical integration would also be uncompetitive, if substantial competition merely resulted in the oligopolists' scope of action being narrowed down considerably *visa-à-vis* non-integrated competitors in downstream markets (BKartA WuW/E 2250 "Hüls-Condea"). If the oligopolists enjoy advantages in competition which outsiders do not have or do not have to the same extent, e.g. a full line of products, possibilities of reciprocal dealing, resource-based advantages, etc., parallel predatory practices to the detriment of outsiders are likely to occur.

Asymmetry of an oligopoly, on the other hand, is not in itself a sufficient indication of substantial competition among the oligopolists, but asymmetrical oligopolies have a greater potential for individual competitive conduct.

Merger that lead to the firms in the oligopoly becoming structurally similar may encourage parallel behaviour. In principle, this applies to *vertical and conglomerate mergers* as well as horizontal mergers (as regards the latter, see II.A.1.b. *supra*).

Vertical mergers resulting in a more balanced degree of vertical integration within the oligopoly as a rule increase the transparency of market conduct. They may also eliminate disruptive suppliers or buyers, which significantly facilitates or safeguards parallel behaviour. Conglomerate mergers may lead to a levelling of resources and thus of retaliatory potentials and thereby encourage conscious parallelism. If all the firms in an oligopoly have competitive advantages after the merger, predatory behaviour is likely to occur.

In exceptional cases, mergers that create greater symmetry of an oligopoly may intensify competition if the firms engaging in competition actually become more competitive in relation to the firms belonging to the oligopoly ("catch-up merger"; KG WuW/E OLG 3081 "Morris-Rothmans").

This applies mainly to vertical and conglomerate mergers as a result of which an oligopoly which is clearly asymmetrical in terms of market shares, market share differences, resources and vertical integration becomes more balanced. Horizontal mergers may improve the conditions of substantial competition within an oligopoly only in very exceptional circumstances, e.g. if there is a distinct asymmetry of market shares bordering on market domination by the merging firms. In principle, the upper limit for horizontal catch-up mergers is a combined market share of 15 per cent (Section 23a (2) sentence 2 of the ARC). In particular, a horizontal merger is very likely to lead to the creation or strengthening of oligopolistic market domination if the merging firms become equal to, or even surpass, the former market leader (BKartA WuW/E 1923 ff. "Burda-Springer"; 1952 f. "Morris-Rothmans").

3. Interlocks

Interlocking directorates or capital links among the firms belonging to an oligopoly will increase the likelihood of conscious parallelism. This applies both to interlocks on the market affected by the merger (a.) and to interlocks on third markets (b.).

a. A market-dominating oligopoly is assumed to exist *prima facie*, i.e. on the basis of an analysis of the competitive conditions alone, if the firms are directly or indirectly (through third firms) interlinked to such a degree that one firm can control all the others.

If firms are interlinked to such an extent, there will be no substantial competition because this might harm the interlinked firms (BGH WuW/E 2240 "G+J-Zeit"; KG WuW/E OLG 4106 "w+i-Weiss-Druck"). The same applies where the firms forming an oligopoly are interlinked through a joint venture that is active on the same market to deter new entry (BGH WuW/E 2195 ff. "Abwehrblatt II").

b. If the firms belonging to an oligopoly are interlinked on third markets either through interlocking directorates or capital links, there is as a rule an increased tendency towards parallel behaviour on the market concerned (spillover effect). Parallel conduct is particularly likely to occur if the cooperation takes place on a neighbouring geographic or a related product market. The same applies if the success of the joint venture is of special importance to the firms belonging to the oligopoly. There is a high likelihood of conscious parallelism if the joint venture operates on a downstream or an upstream market, if this creates uniform buying or selling conditions for the firms forming the oligopoly, and if consequently their scope for competitive action is restricted (BKartA WuW/E 2145 "GfL").

A similar effect on competitive conduct as in the case of interlocks may also occur if the firms form an oligopoly on markets other than the one affected by the merger. If they are also rivals on third markets and if there exists an uncompetitive oligopoly in at least one of those markets, parallel behaviour is likely to occur on the market concerned in the same circumstances as apply in the case of joint ventures operating on third markets.

Similar anticompetitive effects as those resulting from interlocks may come from cartels (BKartA WuW/E 2145 "GfL") or cooperation and customer-supplier relationships among the oligopolists (BKartA WuW/E 2249 "Hüls-Condea").

4. Barriers to market entry see I.5. *supra*.

5. Competition from imperfect substitutes see I.6. *supra*.

6. Foreign competitors see I.7. *supra*.

7. Buying power on the opposite side of the market

In a highly concentrated market, oligopolistic market domination is the more likely, the more fragmented the opposite side of the market is. However, powerful firms on the opposite side of the market may impede conscious parallelism by suppliers.

Large buyers in relation to the entire volume of demand may play off oligopolistic suppliers against each other and cause them to engage in covert competitive action (secret competition). Parallel behaviour may thereby become more difficult or even impossible. This applies in particular to the supply markets of industrial buyers, in particular if demand is irregular and takes the form of large individual orders. On the other hand, large buyers will provoke conscious parallelism. In spite of the presence of large buyers, parallel behaviour is therefore very likely to occur in the case of homogeneous products in general, and in the case of heterogeneous products if there is a high degree of concentration among suppliers and if barriers to market entry are very high.

If the oligopoly of suppliers is virtually faced by only one buyer on the opposite side of the

market, the same principles apply as in relation to single-firm market domination (see I.8. supra.).

8. Market phase see I.9. supra.

9. Overall appraisal of the competitive conditions

All relevant competitive conditions on the market concerned have to be assessed in determining whether oligopolistic market domination is likely to occur.

Even if an analysis of the relevant conditions of competition suggests that not all of them point to oligopolistic market domination, it may nevertheless be likely, subject to an examination of the competitive process. In this analysis, all the competitive conditions speaking in favour of that assumption must be compared with those speaking against it. In doing so, the possibilities of conscious parallelism and the likelihood that such conduct will actually occur after the merger have to be assessed in relation to each other. Special attention should be paid to the significant criteria market share and barriers to entry, for these are a necessary condition of parallel behaviour. The greater the likelihood of parallel behaviour appears on the basis of those criteria, the more evidence is needed to rebut that expectation. Interlocks and the market phase are also important criteria.

Where the pre-requisites for presuming an oligopoly are met (Sections 22 (3) No. 2, 23a (2) of the ARC), it has to be examined whether, on balance, the relevant conditions of competition clearly indicate that substantial competition will be maintained. As regards the rebuttal of that presumption, the same evidentiary requirements must be met - in the opposite sense - as for the presumption of a market-dominating position. The same standards apply to non-prohibition and prohibition of a merger.

If besides the central criteria market share and barriers to entry certain other competitive conditions exist and are combined with the former, making parallel behaviour very likely, other conditions of competition must be assessed only insofar as they would counteract such behaviour. An example of such a combination of competitive conditions is the coexistence of a tight oligopoly, homogeneous bulk commodities, a transparent market, a stagnant or mature market phase, and high barriers to market entry.

A merger does not alter all the conditions of competition on the market concerned to such an extent that their post-merger appraisal would be totally different from that before the merger. In determining whether oligopolistic market domination will be created, it is decisive whether at least some of the competitive conditions will be changed so greatly by the merger that the existing level of competition will no longer be ensured in future. This may be the case, e.g., if overall concentration increases significantly in the presence of barriers to entry. Evidence of substantial competition before the merger is therefore at most an indication of what may be expected after the merger (KG WuW/E OLG 3072 "Morris-Rothmans").

If as a result of examination of the conditions of competition it appears that there is no sufficient likelihood of an anticompetitive oligopoly, the competitive process need not be analysed.

B. Competitive process

An assessment as to whether there is substantial competition within the oligopoly on the market affected by the merger is to be made on the basis of the parameters of competition actually used by the enterprises concerned. Provided all crucial functions of competition are fulfilled on account of the use of parameters, and, in particular, the firms' ability to raise prices remains limited, substantial competition is present (BGH WuW/E 1828 "Tonolli").

1. In the case of homogeneous products, no competition in quality (or only very limited competition in quality) can take place, because the goods supplied by different manufacturers do not show any differences that are of importance in the eyes of buyers. In view of the oligopolistic

interdependence which allows no significant price differences, it is not possible in the majority of cases to determine with reasonable certainty in oligopolistic markets whether there is price competition. In such markets it is therefore all forms of residual price and quality competition as well as factors of minor importance such as competition in services, terms and the provision of advice to customers which decide whether competition is still substantial.

For competition to be substantial it is not sufficient that enterprises make use of the scope of action which is available in markets with homogeneous products. Rather, the intensity and significance to the market of the actual use of parameters altogether must be such that competition is workable (BGH WuW/E 2028 "Texaco-Zerssen"). Substantial competition is not likely to exist, if the firms operating in the market concerned artificially further increase the market transparency typical of homogeneous products markets, e.g. by open price systems and delivered-price systems (BKartA WuW/E 2299 f. "Heidelberger-Zement Malik") or through the so-called "Englische Klausel" (BKartA WuW/E 2321 "Messer Griesheim-Buse").

2. In the case of heterogeneous products, competition in terms of price and quality is possible and a major factor in establishing the presence of substantial competition.

If uniform pricing decisions by the oligopolists are observed over time, competition is no longer substantial, unless an innovative, dynamically developing product is concerned. Price competition at the distribution level is not substantial, if the demand at that level is controlled by consumer preferences as a result of supplier advertising. Interbrand, advertising and R&D competition counts only in connection with competition in quality (KG WuW/E OLG 3074 f. "Morris-Rothmans"). Inter-brand and advertising competition which only relates to intangible product characteristics is a form of predatory competition and therefore not substantial (BKartA AG 86, 380 f. "NUR-ITS").

3. If a review of the competitive process does not provide clear evidence of the presence of substantial competition, a market-dominating oligopoly can be assumed to exist, if the conditions of the oligopoly presumption are satisfied - subject to a review of the relationship between the oligopolists and outsiders (C. infra.) -, provided the conditions of competition prevailing in the market concerned confirm the presentation of a least are not in conflict with it (KG WuW/E OLG 3071 "Morris-Rothmans"; case of "*non liquet*").

4. Even if substantial competition is found to exist in the market, oligopolistic market domination may be present, if such competition takes place only temporarily or locally (BGH WuW/E 2030 "Texaco-Zerssen") or is of a predatory nature. Indicia thereof may, e.g., be exchange rate fluctuations, cyclical excess capacities (BKartA WuW/E 1575 "Kaiser-VAW"), uniform defensive behaviour adopted by the oligopolists against newcomers (KG WuW/E 3078 "Morris-Rothmans") or competitive advantages the oligopolists have over outsiders (see C. infra.).

C. Relationship between oligopolists and outsiders

Provided outsiders operate in the market affected by the merger besides the oligopolists, the assumption of oligopolistic market domination also requires an absence of substantial competition or a presence of a paramount market position of the oligopoly as far as the relationship between the oligopolists and outsiders is concerned.

The examination as to whether the oligopoly has a paramount market position corresponds to that for single-firm market domination (see I. supra.). For that purpose, the totality of the oligopolists take the place of the single firm.

The question of whether there is substantial competition in the relationship between the oligopolists and outsiders has to be examined on the basis of the same criteria as apply to the examination as to whether substantial competition exists within the oligopoly (see II.B. supra.). If it was not found to exist within the oligopoly, substantial competition as a rule is not likely to be present either in the relationship between the oligopolists and outsiders. For conscious parallelism to cannot be sustained indefinitely within the oligopoly, if there is substantial competition from outsiders. If, in spite of parallel behaviour by the oligopolists, there is substantial competition in the relationship between the oligopolists and outsiders, it may be a form of predatory competition. Predatory competition is particularly likely to exist, if the oligopolists enjoy competitive advantages over outsiders (cf., e.g., BKartA WuW/E 1923 ff.).

"Burda-Springer"; AG 86, 380 f. "NUR-ITS").

An overall assessment of the respective results is necessary to complete the review of the conditions of competition, the competitive process and - if necessary - the competitive relationship between the oligopolists and outsiders.

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